Gaz Métropolitain

Connecting with
the future

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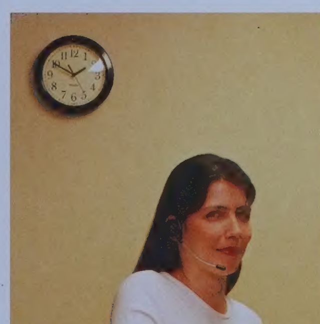
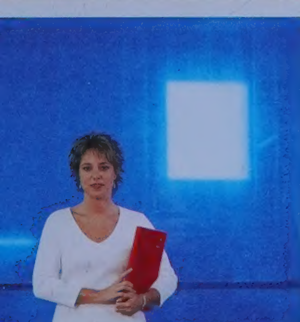
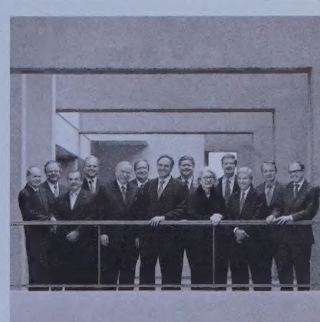
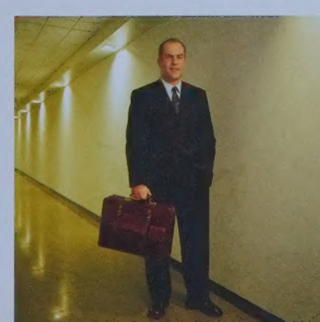
# YOUR ENERGY OUR TEAM

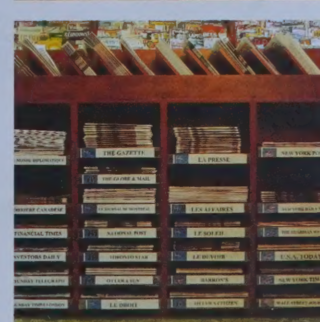
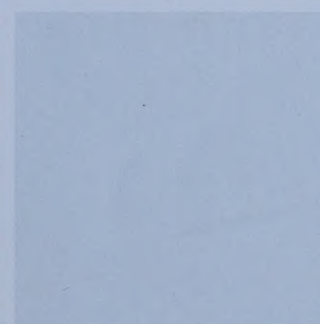


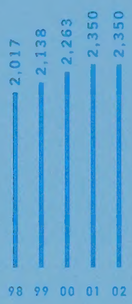
2002
ANNUAL
REPORT

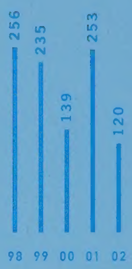


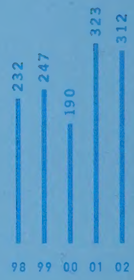
TOTAL ASSETS
(IN MILLIONS OF DOLLARS)




CAPITAL EXPENDITURES AND DEFERRED CHARGES
(IN MILLIONS OF DOLLARS)

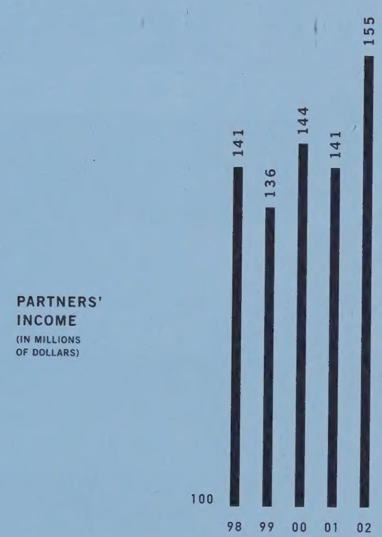



CASH FLOWS PROVIDED BY OPERATIONS
(IN MILLIONS OF DOLLARS)




| Years ended September 30 (in millions of dollars, except for unit data which are in dollars) | **2002** | 2001 |
|---|---|---|
| **CONSOLIDATED INCOME AND CASH FLOWS** | | |
| Revenues | **$1,608** | $2,070 |
| Gross margin | **$ 556** | $ 537 |
| EBITDA (1) | **$ 379** | $ 370 |
| Partners' income | **$ 155** | $ 141 |
| Cash flows from operating activities (before working capital) | **$ 286** | $ 297 |
| Capital expenditures and deferred charges | **$ 120** | $ 253 |
| Diluted and basic Partners' income per unit | **$ 1.40** | $ 1.28 |
| Cash flows per unit from operating activities (before working capital) | **$ 2.59** | $ 2.69 |
| Distributions paid per unit | **$ 1.28** | $ 1.27 |
| Weighted average number of units outstanding (in millions) | **110.5** | 110.5 |
| Interest coverage on consolidated long-term debt over a period of 12 months (times) | **2.85** | 2.51 |
| **CONSOLIDATED NORMALIZED VOLUMES (2)** (in millions of cubic metres) | | |
| MARKETS | | |
| Industrial | **3,263** | 3,023 |
| Commercial | **1,971** | 1,910 |
| Residential | **739** | 743 |
| Total | **5,973** | 5,676 |
| **OTHER INFORMATION** | | |
| Authorized rate of return on deemed common equity | **9.69%** | 10.38% |
| Credit ratings | | |
| Long-term bonds (S&P/DBRS) | **A/A** | A/A |
| Commercial paper (S&P/DBRS) | **A-1 (low)/ R-1 (low)** | A-1 (low)/ R-1 (low) |
| Market prices on Toronto Stock Exchange (in dollars): | | |
| High | **$18.32** | $16.90 |
| Low | **$16.28** | $14.80 |
| Close | **$18.10** | $16.35 |
| Public ownership in Partnership | **22.6%** | 22.6% |
| **CONSOLIDATED BALANCE SHEET** | | |
| Total assets | **$2,350** | $2,350 |
| Long-term debt, including current portions | **$1,241** | $1,270 |
| Partners' equity | **$ 823** | $ 812 |
| Partners' equity per unit | **$ 7.45** | $ 7.35 |
| Net tangible asset coverage on total consolidated long-term debt, including current portion (times) | **1.64** | 1.61 |

(1) Earnings before interest, taxes, depreciation and amortization.
(2) Estimated volumes at normal temperatures in Québec only.




With its flexibility and vitality, Gaz Métropolitain is capable of meeting major challenges and reaching unprecedented levels of efficiency, innovation, expertise and reliability. Moreover, its know-how enables the partnership to pursue activities that are related or similar to its core business. For Gaz Métropolitain, being "in business" is a real commitment. This means offering diversified, competitive and high quality products and services that meet the needs of present and potential customers as well as being a prosperous company where investors, employees and partners stand to gain. Our results prove it!


THE GAZETTE
LA PRESSE
THE GLOBE & MAIL
LE JOURNAL DE MONTREAL
LES AFFAIRES
NATIONAL POST
LE SOLEIL
TORONTO STAR
LE DEVOIR
OTTAWA SUN
BARRON'S
LE DROIT
OTTAWA CITIZEN
U.S.A.
YOUR CONFIDENCE IN US HAS BEEN REWARDED
BY A TOTAL RETURN OF 18.8%

"The company needs financing to grow and develop, and thus it needs investors. My role is to establish a relationship of trust with them. That has to be built over time, with thoroughness, integrity and honesty. I keep them informed about the company's results and about growth opportunities. Investors appreciate getting the facts. Their confidence has been rewarded by continuous growth over the years."

"At Gaz Métro, we are underground specialists. This know-how is very much appreciated, especially by those in charge of municipal services. I make an effort to listen to their needs, to really understand their concerns. That's how our affiliated companies can develop original and economical solutions that enable them to do more at a lower cost."

**STEVE PILON** Senior Advisor, Investor Relations, Treasury

**FRANCIS LEBUIS** Senior Advisor, Water, Finance

"Every day, I have the opportunity to talk to about 50 customers. I answer their questions regarding their Gaz Métro bill, about appliances, products and services. With customers files accessible from my desktop and thanks to ongoing training, I am able to give them precise answers. Helping people is always a pleasure for me."

"I take care of 28 customers and what customers! They represent some 3,500 establishments that belong to restaurant or supermarket chains. I keep in touch with them to help them improve their competitiveness. I work with them in developing new banners and I recommend solutions that respond to all their energy needs."

**SYLVIE NOTTE** Customer Service Representative, Laurentians

**RAYMOND GAULIN** Advisor, Corporate Accounts, Food and Restaurants, Residential, Commercial and Business Partners Division


CONCERN FOR OUR CUSTOMERS IS BEHIND EVERYTHING WE DO—THAT'S WHY MORE THAN 87% OF THEM ARE SATISFIED WITH THE SERVICE WE OFFER
*According to a survey conducted in Spring 2002 by SOM.

OUR **1,200** EMPLOYEES
DO THEIR UTMOST EVERY SINGLE DAY
TO ENSURE OUR SERVICE IS COMPETITIVE
AND TO HELP THE PARTNERSHIP GROW

"I'm very proud of my team of meter readers — one woman and eight guys, all courteous and friendly. They represent Gaz Métro well in their contacts with customers. Thanks to them, nearly 98% of our customers are billed in compliance with our meter-reading policy. It's an important contribution to customer satisfaction."

"For customers out there, I am Gaz Métro — and that's quite a responsibility! At the wheel of my truck, courtesy is my most important tool. In the case of an emergency, I have to stay calm and establish priorities. It's very rewarding work since I get to fix people's problems. And, best of all, my duties are varied and I work outdoors — and that's great!"

**JOSÉE BOUTHILLIER** Supervisor, Meter Reading, Logistics Operations Division

**JEAN-FRANÇOIS COULOMBE** Operations technician, Montréal East, Montérégie and Eastern Townships Regional Division

# VISION, VALUES AND COMMITMENTS

## CORPORATE VISION

In carrying out its mission and pursuing its objectives, Gaz Métropolitain aims for excellence.

Proud of their organization and of their occupation, employees, both individually and collectively, strive to surpass themselves. They do not take the easy way out and seek continuous improvement in their performance to satisfy the needs and expectations of customers, investors and business partners, as well as to create a corporate image that is beyond reproach.

To motivate its employees, Gaz Métropolitain provides working conditions that are competitive, and an enviable quality of work life and worthwhile professional development programs, all within a participatory management environment where, in line with common objectives, creativity, initiative and individual accountability are encouraged.

CORPORATE POLICY – NOVEMBER 15, 2000

## CORPORATE VALUES

The primary principle underlying Gaz Métropolitain's Code of Ethics and other policies is expressed in one fundamental value: respect.

### RESPECT FOR CUSTOMERS

The Partnership's "raison d'être", customers expect products and services that meet their needs in terms of quality and price.

### RESPECT FOR INVESTORS

As source of capital for the Partnership, investors are looking for a return that compares favourably with similar companies.

### RESPECT FOR EMPLOYEES

The driving force between the Partnership's investors and customers, employees count on being provided with remuneration and working conditions that will ensure their continued loyalty, and a work atmosphere where health and safety are a priority and where harassment is not tolerated.

Respect for employees also involves systematic, transparent communication, participatory management, encouragement for professional development and recognition of achievements.

### RESPECT FOR SUPPLIERS AND BUSINESS PARTNERS

Stakeholders in the success of the Partnership, suppliers and business partners assume they will be treated respectfully and equitably, with a view to mutual success.

### RESPECT FOR REGULATORY AUTHORITIES

Guardians of the balance of relations between a company that carries on an exclusive business activity and its customers, regulatory authorities, as well as the organizations that appear before them, are entitled to relevant, transparent information from the company as well as an attentive ear to their expectations.

### RESPECT FOR COMPETITORS

Essential players in a market economy, companies that play fair are entitled to expect that their products and services will be judged on their merits.

### RESPECT FOR THE COMMUNITY

Ultimate judge of the Partnership's reputation, the community demands public safety, protection of the environment and corporate conduct that is in line with what is expected of any good citizen.

CORPORATE POLICY – NOVEMBER 15, 2000

## CORPORATE COMMITMENTS

Gaz Métropolitain is committed to developing and maintaining the highest ethical and business standards, in our relations with customers, suppliers, business partners, investors, regulatory bodies, competitors, the community and employees. These commitments can be summarized as follows:

### TO CUSTOMERS

We are committed to providing high quality goods and services at reasonable prices. Customers will be treated with the utmost consideration, with an open mind and in good faith.

### TO SUPPLIERS

We are committed to treating our suppliers equitably. Refraining from any discrimination and acting in a transparent manner, we encourage competition, while promoting long-term business relations.

### TO BUSINESS PARTNERS

We are committed to identifying and promoting mutual interests with our business partners. Both parties have to benefit from the synergies that come from an alliance.

### TO INVESTORS

We are committed to complying with the highest standards of corporate governance, prudently managing the Company's assets and resources and striving to generate a return that compares favourably with returns earned by similar companies.

We are also committed to ensuring that the Company's books and records, as well as information published for investors, accurately reflect the Company's financial position.

### TO REGULATORY BODIES

We are committed to acting in a respectful and transparent manner toward the *Régie de l'énergie* and other regulatory bodies, as well as toward intervenors that appear before these bodies.

### TO COMPETITORS

We are committed to developing the Company's business through vigorous but fair competition, emphasizing the benefits of our products and services.

### TO THE COMMUNITY

We are committed to respecting laws and standards and, in particular, to ensuring that the transmission and distribution system is safe. We are also committed to demonstrating leadership, self-discipline and determination in the pursuit of our environmental actions with a view to making an optimal contribution to the community. We are committed to improving the well-being of the community, in particular through philanthropic works and by encouraging employees to participate in community work.

### TO EMPLOYEES

We are committed to providing employees with a work atmosphere that is respectful of their health and safety and free from harassment. Employees will be treated with respect and dignity, regardless of their age, ethnic background, sex, sexual orientation, religion, marital status or handicap, if any.

### TO ALL PUBLICS ABOVE-MENTIONED

We are committed to:

- Carrying out our duties with the utmost integrity;
- Respecting any express or implicit agreements;
- Assuming responsibility for our actions;
- Ensuring personal, confidential or privileged information is protected;
- Communicating in an honest and forthright manner.

CODE OF ETHICS EXTRACT – NOVEMBER 15, 2000

### Mr. J. RICHARD BIRD

Before joining Enbridge in 1995, Mr. Bird held senior finance and corporate development positions with Gulf Canada Resources and GW Utilities. He is presently Group Vice President, Transportation North for Enbridge. He joined Enbridge as Vice President and Treasurer following which he was appointed Senior Vice President, Corporate Planning and Development.

**Director since** August 19, 1998
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 4/6

### Mr. JEAN-GUY DESJARDINS

Mr. Desjardins is the President and Chief Executive Officer of Fiera Capital, which he founded in 2002. He was also the co-founder and main shareholder of TAL Global Asset Management Inc. until it was taken over by a financial institution. Mr. Desjardins was the President and Chief Executive Officer of TAL from 1987 to 2001. He is a member of a number of associations and boards of directors, including the boards of the Laurentian Bank of Canada and the *École des Hautes Études Commerciales*.

**Director since** August 22, 2002
**Number of units held** [(1)] 55,000
**Attendance at meetings** [(2)] Committee: 1/1

### Ms. NICOLLE FORGET

A graduate of the *Université du Québec à Montréal*, the *École des Hautes Études Commerciales* and the *Université de Montréal*, Ms. Forget is a member of the Quebec Bar. She has been a member of a number of administrative tribunals and boards of directors, including the boards of Hydro-Québec and the Economic Council of Canada. She is a member of, among others, the board of directors of the Jean Coutu Group and F Capital.

**Director since** January 30, 1997
**Number of units held** [(1)] 1,500
**Attendance at meetings** [(2)] Board: 6/6
Committees: 10/10

### Mr. LOUIS P. GIGNAC

Mr. Gignac has been the President and Chief Executive Officer of Cambior Inc. since 1986. Cambior produces gold and niobium in Québec and South America. The Company has approximately 1,650 employees. Mr. Gignac, who holds a doctorate in mining engineering, is also a director of Domtar.

**Director since** September 25, 1990
**Number of units held** [(1)] 1,000
**Attendance at meetings** [(2)] Board: 6/6
Committees: 6/6

### Mr. MICHEL GOURDEAU

From 1985 to 1997, Mr. Gourdeau was Vice President, Gas Services for Gaz Métropolitain. He left to join Hydro-Québec as Executive Vice President – Energy Services prior to his appointment as Executive Vice President – Natural Gas Sector in 1999.

**Director since** February 2, 2000
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 4/6
Committee: 3/5

### Mr. EMMANUEL HEDDE

Mr. Hedde joined the Subsidiaries and Financial Interests Division of Gaz de France in 1993, prior to which he had held various management positions with a finance company for 13 years. Mr. Hedde was appointed Executive Vice President, Finance Division of Gaz de France in 2000.

**Director since** May 23, 2002
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 1/1

### Mr. PHILIPPE HOCHART

Presently Gaz de France's Representative for North America, Mr. Hochart has been with the Company since 1980 where he has held executive positions in the distribution, rate setting, gas supply, transportation, finance and treasury sectors, as well as natural gas trading.

**Director since** February 6, 2002
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 5/5

### Mr. JACQUES LAURENT

Mr. Laurent is a lawyer. He is Chairman of the Board of Hydro-Québec since 2001. He is also a director of Domtar, Chairman of the Board of the *Orchestre symphonique de Montréal* and a Governor of the National Theatre School of Canada.

**Director and Vice Chairman of the Board since** February 6, 2002
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 5/5
Committee: 0/1

### Mr. STEPHEN J.J. LETWIN

Before joining Enbridge, Mr. Letwin was, among others, Senior Vice President and Chief Financial Officer with TransCanada PipeLines and, prior to that, President and Chief Financial Officer of Numac Oil & Gas. In 1999, he was appointed President and Chief Operating Officer of Energy Services Enbridge until 2000 when he was appointed Group Vice President, Distribution and Services of Enbridge Inc.

**Director since** February 7, 2001
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 5/6
Committee: 4/5

### Mr. GASTON LONGVAL

Mr. LongVal retired from Gaz Métropolitain in 1996 after 36 years of service. At the time of his retirement, he was Assistant to the President and Vice President, Human Resources, positions he held since 1988. With a technological education in applied sciences, and later in industrial relations, he was also Vice President, Human Resources from 1977 to 1982, following which he was Vice President, Operations from 1982 to 1987.

**Director since** February 6, 2002
**Number of units held** [(1)] 2,000
**Attendance at meetings** [(2)] Board: 5/5
Committee: 3/3

### Mr. MICHEL MARUENDA

Mr. Maruenda's professional career started at Électricité de France in 1975, following which he worked for Saur International and Groupe Saur from 1994 until 2000, when he was appointed Deputy Executive Vice President, Gas Distribution Division with Gaz de France. Mr. Maruenda was recently put in charge of an important reorganization of natural gas distribution in France as Deputy Executive Vice President.

**Director since** November 15, 2000
**Number of units held** [(1)] –
**Attendance at meetings** [(2)] Board: 3/6

### Mr. ROBERT PARIZEAU

For the past few years, following 20 years at the head of Sodarcan Inc, an insurance, reinsurance and actuarial consulting company, Mr. Parizeau has been a corporate director. He is the Chairman of the boards of AON Parizeau and Gaz Métropolitain, and a director of, among others, the National Bank of Canada, National Bank Financial, Power Corporation, the Canam Manac Group and Van Houtte.

**Director since** September 25,1990
**Number of units held** [(1)] 10,000
**Attendance at meetings** [(2)] Board: 6/6
Committees: 15/15

### Mr. RÉAL SUREAU

Mr. Sureau, an accountant by profession, is President of Gestion Sureau Limitée and, since 1995, Vice President of the Patented Medicine Prices Review Board. Over the course of his career, positions held by Mr. Sureau include Vice President, Finance with Forex and the Canam Manac Group. He was also President of the *Ordre des comptables agréés du Québec* in 1995-1996. He sits on the boards of directors of TAFISA Canada and Company Ltd., Gestion de placements Valorem Inc. and Institut de réadaptation de Montréal.

**Director since** January 26, 1995
(was also a Director from 1987 to 1991)
**Number of units held** [(1)] 5,000
**Attendance at meetings** [(2)] Board: 6/6
Committees: 14/14

### Mr. ROBERT TESSIER

Mr. Tessier has been employed as the President and Chief Executive Officer of Gaz Métropolitain since 1997. He started his career in the public sector where, among others, he was the Vice Rector of the *Université du Québec*, Secretary of the *Conseil du Trésor du Québec*, Deputy Minister in the *Ministère de l'Énergie et des Ressources*, and Executive Vice President of *La Société générale de financement*. From 1991 to 1992, he was President and Chief Executive Officer of MIL Group and, from 1992 to 1996, of Alstom Canada.

Mr. Tessier chairs the boards of the Canadian Gas Association and the Montréal Heart Institute. He is also a director of AXA Canada and Investors Group Corporate Class Inc.

**Director since** January 30, 1997
**Number of units held** [(1)] 13,500
**Attendance at meetings** [(2)] Board: 6/6

(1) A Director who does not personnally receive the director's remuneration does not have to own Partnership's units. Otherwise, the minimum is 1,000 units and will be 2,000 in 2004.
(2) Meetings during fiscal 2002.

FROM LEFT TO RIGHT: GASTON LONGVAL, MICHEL GOURDEAU, JACQUES LAURENT, JEAN-GUY DESJARDINS, ROBERT PARIZEAU, LOUIS P. GIGNAC, ROBERT TESSIER, STEPHEN J.J. LETWIN, NICOLLE FORGET, J. RICHARD BIRD, RÉAL SUREAU, MICHEL MARUENDA, PHILIPPE HOCHART, EMMANUEL HEDDE (ABSENT)

# REPORT TO PARTNERS

The Directors, officers and employees are proud to present this 45th Annual Report, the 10th since Gaz Métropolitain was organized as a limited partnership in which the public could invest. And if the price of the unit over the past year is any indication, Partners' expectations have been satisfied at a time when stock markets have had the wind taken out of their sails following the excesses of the 1990s. The S&P/TSX, the main Canadian stock market index, fell 9.6% between September 30, 2001 and September 30, 2002, while the price of Gaz Métropolitain's unit increased by 10.7%, from $16.35 to $18.10.

Why such a strong performance? Apart from the excellent financial results that are discussed further on and favourable long-term interest rates, there are three reasons: a strong and dependable business, with an appropriate corporate structure, that provides structural assurances of effective corporate governance. A strong and dependable business because, unlike other businesses whose stocks were at one point stock market picks, Gaz Métropolitain:

- Has been in existence for decades;
- Operates tangible assets;
- Under the oversight of regulatory bodies, provides transportation and distribution services for natural gas, an energy source whose qualities are recognized worldwide and whose popularity continues to grow; and
- Year after year, generates for investors relatively stable and generally foreseeable earnings.

Secondly, Gaz Métropolitain's corporate structure is suitable for the nature of its activities and for a given investor profile, i.e. investors for whom a steady return is more important than capital appreciation, although capital appreciation is by no means ignored. The limited partnership structure allows:

- Gaz Métropolitain to record Partners' income before income tax and distribute to the Partners their pro rata share of these earnings, and
- Partners who elect to hold the units in an RRSP type portfolio to get a return on the before pre-tax distribution they receive.

Last year, as always, prudent investors had to include in their portfolios securities from a business that not only systematically produces earnings, but also distributes them virtually in their entirety (97% on average in the last five years).

And the third reason why the unit performed so well over the past year—governance. Corporate governance can be summarized as the manner in which the Directors discharge their prime responsibility of overseeing the management of the affairs of the organization. The main factors that should reassure investors are listed on the next page, if indeed they require any reassurance. Further details are provided in the Statement on Corporate Governance Practices on page 62 of this Annual Report.

- The General Partner, Gaz Métropolitain, inc., which is responsible for managing the Partnership, holds 77.4% of the units, which means it has a vested interest in its performance.
- The Directors are senior officers of corporations that are shareholders of Noverco (Hydro-Québec, Enbridge and Gaz de France), and other individuals who have extensive business experience. The Partnership's President and Chief Executive Officer is the only member of the Board of Directors who is also an employee.
- The Directors possess a broad range of skills and experience.
- The Chairman of the Board has no connection, other than by virtue of his position, to management or the shareholders of Noverco.

Furthermore, the main activities of the Partnership and the businesses in which it holds significant interests are monitored by regulatory bodies, which adds another layer of protection for investors.

## 2002 IN REVIEW

In the November 15, 2001 Report to Partners, we stated that "since the terrorist attacks against the United States, the economic slowdown that was already underway is verging on recession" and that "it would therefore be unwise to be overly optimistic about what the 2002 year has in store..." Quite obviously, our predictions for the future were pessimistic, as were those of most forecasters on Canada's economy. In 2002, Gaz Métropolitain had its best year ever in terms of Partners' income — $154.6 million, i.e. $1.40 per unit, which represents a 9.5% increase over the $141.2 million, or $1.28 per unit, earned in 2001.

This performance is the result not only of a better economic context than in 2001, when gas prices showed unprecedented volatility, but also of an organization that continues to be more effective in the use it makes of its assets and in the management of its investment interests. Every sector did well and contributed to the $13.4 million increase in income.

Income from the core business, the distribution of natural gas in Québec and Vermont, is $7.5 million higher than the preceding year, with normalized volumes (for temperatures) up by 5.2% to 5,973 million cubic metres. This increase is primarily attributable to the interruptible service market where customers took advantage of savings opportunities arising from the occasional favourable competitive position of natural gas in relation to heavy fuel oil. The Partnership takes a proactive approach in this area, with its sales representatives bringing market opportunities identified by Gas Supply personnel to the attention of customers. Interested customers can then sign contracts ranging from a few weeks to several months with Gaz Métropolitain and with natural gas suppliers of their choice.

Transportation and load balancing optimization transactions also contributed to increased income. Again, Gas Supply personnel are continuously on the lookout for potential short-term transactions that will make the best possible use of these tools at any given time. All in all, the Partnership generated overearnings of $27.1 million in its Québec distribution activity. The performance incentive mechanism approved by the Régie allows the Partnership to retain one-third of this amount, i.e. $9.0 million, with the balance being credited to customers ($12.8 million) and the Energy Efficiency Fund ($5.3 million).

We would be remiss if we did not mention the ongoing strong performance of Vermont Gas for the 15 years that it has been part of our corporate family. Year after year, it performs well even when much milder than normal temperatures affect its deliveries and revenues, as was the case in 2002. Vermont Gas distinguished itself through judicious management of its supply and tight cost controls.

REPORT TO PARTNERS

The year 2002 was a very busy one for the second largest sector of activity, i.e. the transportation sector. The partners of TQM Pipeline, a partnership that is owned 50-50 with TransCanada PipeLines, pursued the corporate streamlining that has been underway for the past few years in order to provide additional benefits for customers and owners. For historical reasons, TQM Pipeline, which is in fact a subcontractor of TCPL, had its own independent organization. Following discussions with management and consideration of a number of scenarios, the partners agreed to reduce TQM Pipeline's personnel to a bare minimum and to indirectly give TCPL the responsibility for managing the system. TCPL already operates in Québec. TQM's employees were informed of the reorganization on October 31.

The issue for PNGTS, a transportation system in New England in which the Partnership holds an indirect interest of 20.7%, was much more significant. Constructed on the basis of rates that were frozen until March 2002, PNGTS had to obtain, effective April 2002, rates that would reflect its investments and generate a reasonable return on shareholders' equity. The filing of an application in this regard with the Federal Energy Regulatory Commission was followed by intense negotiations between PNGTS and its customers, which culminated in a unanimous agreement that was submitted to the FERC on October 25. If, as expected, it is approved by the FERC, the firm service transportation rate would increase by approximately 35% and would generate the reasonable return expected by the owners.

For the year 2002, the transportation sector contributed $2.5 million to the increase in Partners' income over 2001. The only cloud is that the Cartier Pipeline project had to be suspended. As the East Coast basin has yet to show that it could produce additional volumes for 15 or 20 years, it became premature to get into a rate methodology debate for a gas pipeline that would not be constructed without the assurance of long-term supply. Gaz Métropolitain and Enbridge, the project promoters, will monitor the exploration and production activities in this region so as to be prepared to revive the project at the appropriate time.

The Partnership's third major sector of activity includes the energy services provided by Gaz Métropolitain Plus and its subsidiaries as well as other unregulated activities. Overall, this sector eliminated a loss of $1.3 million in 2001 and broke even in 2002. This turnaround is due essentially to Gaz Métropolitain Plus, a company that has been operating as an independent organization for only two years, and Aqua Data and Aqua-Rehab, two companies that are well positioned to help municipal governments diagnose and, if necessary, rehabilitate their water and waste water systems. Other companies in this sector are also doing well, in particular Cable VDN with its fibre optic network and TelDig, which develops and markets software for locating pubic service infrastructures.

In terms of business development, the main effort focused on cogeneration plant projects developed with Boralex as our partner in connection with a call for tenders by Hydro-Québec, Distribution Division. Unfortunately, these projects were not retained, as Hydro-Québec selected proposals from its Production Division and a combined cycle gas plant project from another developer. Gaz Métropolitain will even so benefit from the latter project, because it will have a new large firm service natural gas customer.

We conclude this brief review with a few comments about the development of the organization responsible for natural gas distribution in Quebec and which, it has to be acknowledged, has had a large number of demands placed on it by the initiatives for change over the past years. Management has opted for transparency and partnership, the keys to getting personnel to buy in to common objectives for such projects as the total quality initiative, where significant progress has been made, the development and implementation of an enterprise resource management system and an orderly reduction of nearly 150 regular positions over a period of little more than one year.

**ANDRÉ BOULANGER**
Vice President, Sales, Marketing and Customer Services

**SERGE RÉGNIER**
Vice President, Human Resources and Quality

**STÉPHANE BERTRAND**
Vice President, Communications, Public and Governmental Affairs

**RENÉ BÉDARD**
Corporate Secretary

**ROBERT TESSIER**
President and Chief Executive Officer

**JACQUES CHARRON**
Vice President, Operations

**LUC SICOTTE**
Vice President and Chief Financial Officer

**SOPHIE BROCHU**
Vice President, Business Development and Gas Supply

**PIERRE DESPARS**
Vice President, Corporate and Legal Affairs

## MANAGEMENT COMMITTEE









REPORT TO PARTNERS

The mutual respect that has developed over the years with union representatives, and the employees they represent, has meant that the blue-collar workers' activities could be reviewed and significantly reorganized after lengthy but productive negotiations for the collective agreement that was renewed until September 2005. Initial discussions for the renewal of the white-collar workers' collective agreement have begun in the same spirit.

We have adopted the principle put forward by the *Mouvement Québécois de la qualité* that an organization that wants to perform well has to satisfy its three cornerstones—customers, investors and employees. All of our initiatives for change are focused on this principle and we would like to express our appreciation to our employees for sharing this view and for showing it more and more through their day-to-day activities.

Major investments over the past few years in modernizing management information systems, in developing more efficient procedures and methods, and in mobilizing personnel across the entire organization have resulted in increased productivity, lower construction and operating costs, increased sales and enhanced customer service. Performance indicators allow us to adjust our approach as required in order to achieve our objectives in each of these areas.

## OUTLOOK FOR 2003 FISCAL YEAR

Despite an uncertain economic situation in the United States, Canada and Québec are likely to be spared, at least for a while. Therefore, barring any major unforeseen change in the competitive situation, natural gas distribution should continue to perform well. The outlook for more widespread use of natural gas in Québec is promising and the Partnership intends to intensify its efforts to increase its market share. This year, the transportation activity should start to reap the benefits of the changes made at TQM Pipeline and, particularly, at PNGTS. Unregulated activities should maintain their trend and start generating income.

We bring to your attention one factor which affects, and will continue to affect, Partners' income, which is determined on a pre-tax basis as you are aware. The Partnership's Québec distribution activity and TQM Pipeline are authorized by their respective regulatory bodies to recover the current income tax cost they would have had to bear if they were incorporated companies rather than limited partnerships. The federal corporate tax rate was reduced by 2% in 2002 and will continue to decrease at the same rate up to and including 2004. Partners' income in 2002 would have been approximately $4.0 million higher if it had not been for this decrease in the tax rate. There will be a cumulative effect in 2003 and 2004. So before income can grow, the Partnership has to find ways to offset the impact of lower income due to the deemed income tax. We were successful in 2002 and are tackling the challenge for 2003 and 2004.

When the financial results for the year 2002 were released, on this November 20, the Board of Directors announced that the quarterly income distribution would increase from $0.32 per unit to $0.34 per unit on January 1, 2003, thereby expressing its confidence in the short- and medium-term outlook for the Partnership.

Gaz Métropolitain, inc. in its capacity as General Partner
November 20, 2002

**ROBERT PARIZEAU**
Chairman of the Board

**ROBERT TESSIER**
President and Chief Executive Officer

GMi
GAZ MÉTROPOLITAIN INC.

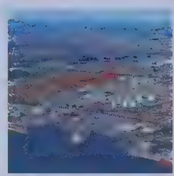
GMCLP
GAZ MÉTROPOLITAIN & COMPANY, LIMITED PARTNERSHIP

TQM
TRANS QUÉBEC & MARITIMES PIPELINE INC.

PNGTS
PORTLAND NATURAL GAS TRANSMISSION SYSTEM

## OWNERSHIP & SECTORS OF ACTIVITY

# THE YEAR IN REVIEW



THE 22 ENERGY EFFICIENCY PROGRAMS ARE INTENDED FOR RESIDENTIAL, COMMERCIAL, INSTITUTIONAL AND INDUSTRIAL CUSTOMERS.

The Report to Partners, as well as Management's Discussion and Analysis, include information specific to the 2002 fiscal year. Over and above these results, Gaz Métropolitain has been active on several fronts during the year, as the following news briefs illustrate.

## SAVINGS SUFFICIENT TO SUPPLY 1,500 HOMES

Gaz Métropolitain's Energy Efficiency Plan helps consumers manage their energy demand efficiently and, as a result, have lower energy bills.

Commended as a good example by the Québec Minister of Natural Resources on their launch at the end of 2001, the 22 energy efficiency programs are intended for residential, commercial, institutional and industrial customers.

A year and a half later, these innovative programs have enabled customers to achieve savings of 4.5 million $m^3$ of natural gas, sufficient to supply 1,500 single-family homes for a year. These savings translate into an annual reduction in greenhouse gas emissions equivalent to 8,483 tonnes of $CO_2$.

## TWO LARGE CUSTOMERS HOOK UP WITH GAZ MÉTROPOLITAIN

Counted among its customers are some 300 large companies on the territory served by Gaz Métropolitain. J. Ford Ltée of Portneuf, which makes specialized papers, joined that count in 2002. The contract, which anticipates consumption of 100 million $m^3$ over 5 years, will enable the company to reduce its current energy bill by 25-30%.

A sizeable contract has also been signed with Interquisa Canada for an annual consumption of 77 million $m^3$. The agreement covers supply to a new petrochemical plant in Montréal East that will produce 500,000 tonnes of purified terephthalic acid per year.

## GAZ MÉTROPOLITAIN A HIT ON THE INTERNET

According to the Secor-Commerce Internet index, which evaluates the 25 best Québec Internet sites designed for consumers, **www.gazmetro.com** came in third, immediately behind bell.ca and desjardins.com.

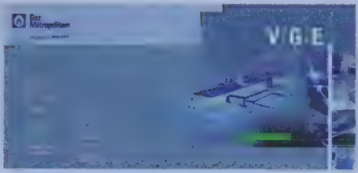
The evaluation uses two sub-indices: the value consumers may get from the site (quality of information, customized products and services, etc.) and user-friendliness (everything that facilitates navigation, such as ergonomics and security functions).

Described as "a must-visit site, dynamic and content-rich" the Gaz Métropolitain Web site is a good reflection of the vitality of the Partnership itself, which is able to achieve excellence with relatively limited resources.

## REAL-TIME DATA EXCHANGE WITH LARGE COMPANIES

The online services available at **www.gazmetro.com** continued to grow in 2002. The most recent service is designed expressly for Gaz Métropolitain's large customers.

They now have secure access to a personalized site called ViGiE, where they can consult historical data on their consumption, their bills, service interruptions, as well as a lot more information, all designed to facilitate their relations with Gaz Métropolitain. This new service has been well received by the large customers market.




### NEW OFFICES OPENED IN MONTRÉAL

The regionalization of operating activities continued during 2002 with the opening of two joint regional/business offices in Montréal. More than 120 employees now occupy the premises, which are equipped and organized to better respond to the needs of their respective customers.

Special attention was paid to the layout of the premises in order to foster communication and teamwork between the different departments. The Sales and Marketing sector has also located some of its teams in the new premises to ensure close cooperation between all those involved in serving the region.

### NEW COLLECTIVE AGREEMENT SIGNED WITH BLUE COLLARS

On May 11, 2002, employees represented by the *Confédération des syndicats nationaux* (C.S.N.) voted in favour of accepting the agreement in principle reached a month earlier by Gaz Métropolitain and their union.

The new collective agreement signals a major change in the way we do things. Employees will have a reduced work week, as well as more satisfying jobs with more varied tasks. In return, the company will gain greater operating flexibility, which will make it more efficient. The climate of trust between the parties, backed by a partnership approach, led to a "win-win-win" settlement for employees, the union and the company.

### DISTRIBUTION SYSTEM EXTENDED IN LOTBINIÈRE REGION

Gaz Métropolitain has completed the construction, within budget and on time, of a 66.6-km extension to its distribution system in the Lotbinière region. This $8.2-million project, long-awaited by the community, especially local business and industry, could not have been achieved without the $6.1 million contribution from the Québec government and the close collaboration of the *Centre local de développement de Lotbinière.*

An exhaustive pilot project to solicit potential customers implemented by Sales and Operations improved the viability of the project by adding customers to those who had been identified initially. And it is also important to note the efficient job done by Ganotec, the general contractor on the project.

### RIGOROUS MANAGEMENT OF COUNTERPARTY RISK

While many players in North America are suffering financial repercussions from the debacle with energy brokers, Gaz Métropolitain has come out unscathed, thanks to its tradition of discipline and vigilance in selecting its natural gas supply partners.

Nevertheless, the Partnership has tightened its risk-monitoring and credit procedures and is being more and more selective when choosing its counterparties, given the financial scale of natural gas activities.

GAZ MÉTROPOLITAIN WAS ABLE TO REACH AN AGREEMENT THAT, FOR THE FIRST TIME SINCE THE PERFORMANCE INCENTIVE SCHEME WAS INTRODUCED, WAS UNANIMOUS AMONG ALL INTERESTED PARTIES.

### GAZ MÉTROPOLITAIN: PARTNERING WITH MUNICIPALITIES

At the end of 2001, Gaz Métropolitain launched an action plan aimed at strengthening its relations with municipalities in order to facilitate approval of development projects. The plan has given rise to two liaison committees: one with the *Fédération québécoise des municipalités*, the other with the *Union des municipalités du Québec*.

The meetings organized by these two committees have helped reach a better understanding of the mutual concerns of the participants and positioned Gaz Métropolitain as an essential municipal partner. The liaison committees have each produced a report on their activities, detailing the discussions held at their meetings. The reports received much acclaim when they were distributed at the UMQ and FQM annual meetings.

### IMPROVED BUSINESS PROCESSES THANKS TO SAPHIR

Gaz Métropolitain seized the opportunity presented by the introduction of SAP software in Fall 2000 to improve its business processes. In October 2001, the implementation of the payroll, human resources, finance, and goods and service procurement modules encouraged the integration of the company's administrative activities, thus contributing to improving overall performance.

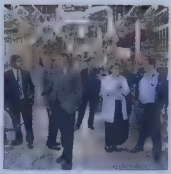
In June 2002, implementation of the functionalities associated with the system maintenance module was preceded by a total review of processes, which helped optimize the timing and sequence of preventive maintenance interventions. The step-by-step implementation by administrative region was finally completed in September 2002.

### UNANIMITY ON TARIFFS

During its review of tariffs for the 2003 fiscal year, Gaz Métropolitain was able to reach an agreement that, for the first time since the performance incentive scheme was introduced, was unanimous among all interested parties. The agreement was presented in June 2002 to the *Régie de l'énergie* (Energy Board), which gave its full approval in September for application effective from October 1, 2002.

This unanimity reflects the climate of the relations between Gaz Métropolitain, customer associations and environmental interest groups. This climate is characterized by mutual respect and comprehension, and supported by the negotiated agreement process introduced by the *Régie de l'énergie*. This is the same process that facilitated the introduction of the performance incentive scheme, under which productivity gains are shared between the Partnership and its customers.

Défi Excellence



THE UNIQUE EXPERTISE OFFERED BY THE SCHOOL'S PERSONNEL AND EQUIPMENT MAKES IT ESSENTIAL IN TRAINING AND DEVELOPING THE LABOUR FORCE FOR THE WHOLE NATURAL GAS SECTOR.

### MAINTAINING ISO 14001 REGISTRATION

Gaz Métropolitain has succeeded once again in maintaining the ISO 14001 registration of its environmental management system. This registration significantly helps maintain and develop environmental awareness among employees, who are encouraged to take concrete action, at home and at work, to protect and improve the environment, especially during Environment Week.

### TOTAL QUALITY INITIATIVE MAKES PROGRESS

In December 2001, Gaz Métropolitain scored 379 points in an evaluation of its performance using the QUALI*meter*, a diagnostic tool recommended by the *Mouvement québécois de la qualité*. This internationally recognized bench-mark enables Québec companies to compare their practices with those of the best companies in the world.

The evaluation, conducted by independent experts, showed significant progress compared with the 235 points scored in 2000 in a self-evaluation. The continuous improvement of business and management processes is Gaz Métropolitain's objective.

### MAKEOVER FOR THE *ÉCOLE DE TECHNOLOGIE GAZIÈRE*

Major renovation and redesign work has resulted in doubling the number of classrooms at the *École de technologie gazière*, as well as in enlarging the laboratory, which now houses more than 250 different natural gas appliances.

These investments will enable the school to meet the training needs of the company's employees, first and foremost, as well as meet a growing demand from partners, companies, fire departments and schools. The unique expertise offered by the school's personnel and equipment makes it essential in training and developing the labour force for the whole natural gas sector. The school hones the skills of current workers and trains the next generation, which contributes to the expansion of the natural gas industry in Québec.

### A LEADER IN OCCUPATIONAL HEALTH AND SAFETY

Thanks to the hard work by all concerned in the last three years, the frequency of work accidents has fallen by more than 30%. Gaz Métropolitain thus ranks first among public-service companies in Québec and is among the best in Canada in its sector of activity.

## SUBSIDIARIES AND AFFILIATED COMPANIES

### *AQUA DATA* EXPANDS INTO THE UNITED STATES

To continue to grow, Aqua Data has focussed its strategy towards the U.S. market by offering products and services that are in high demand. The performance of the Aqua Zoom tele-objective camera in the diagnosis of wastewater collection systems, and the Aqua Data unidirectional flushing of water distribution networks, has resulted in Aqua Data's signing an agreement to enter into the U.S. market.

Last October, Malcolm Pirnie and Aqua Data created InfraMetrix, a joint venture with offices in Boston, Mass., to serve this market.

THE GAZ MÉTROPOLITAIN PLUS GROUP ALSO PURCHASED THE 50% BALANCE OF SHARES IN OPTION GAZ, WHICH SPECIALIZES IN THE DISTRIBUTION OF HEATING EQUIPMENT.

TELDIG

### *GAZ MÉTROPOLITAIN PLUS* PUTS THE LAST TOUCHES ON ITS RANGE OF SERVICES

The Gaz Métropolitain Plus Group has just successfully ended its second full year as an autonomous company. It continued the integration of different parts of the group and acquired Servitech Combustion, which installs and maintains industrial boilers. It also purchased the 50% remaining shares in Option Gaz, which specializes in the distribution of heating equipment. Gaz Métropolitain Plus is now able to offer a complete range of energy services to residential, commercial, institutional and industrial markets throughout Québec.

### *TELDIG SYSTEMS* TARGETS NORTH AMERICA

TelDig Systems is a leader in software programs for infrastructure damage prevention. The only Canadian company in its activity sector, TelDig Systems offers computerized services to manage demands for locating underground networks to the entire North American market.

A pioneer in the use of digital mapping and electronic drawings, TelDig Systems has developed mobile wireless applications so users can work more efficiently in the field. The company recently signed strategic partnership agreements with two California companies that specialize in digital mapping and aerial photography.

### *CABLE VDN* INCREASES PROFITABILITY

Cable VDN continues to make progress as a telecommunications services carrier (video, voice, data). In 2002, its high-capacity fibre optic network attracted key customers from the financial, outsourced IT and telecommunications services sectors, and also signed up residential customers in a pilot project in some parts of Montréal.

GAZ MÉTROPOLITAIN WOULD LIKE ITS COMMITMENT TO GOOD CORPORATE CITIZENSHIP TO BE BETTER KNOWN, AND SO A SECTION OF ITS ANNUAL REPORT IS DEVOTED TO PRESENTING A REPORT ON ITS SOCIAL AND ENVIRONMENTAL ACTIVITIES. THE FOLLOWING PAGES ILLUSTRATE HOW THE PARTNERSHIP'S POLICIES REGARDING ITS COMMITMENT TO THE COMMUNITY AND RESPECT FOR THE ENVIRONMENT ARE EXPRESSED IN CONCRETE WAYS.

# COMMITMENT TO THE COMMUNITY

## CONCERN FOR THE NEEDS OF THE COMMUNITY

Through donations and sponsorships, Gaz Métropolitain aims to contribute to the well-being of the communities it serves. This commitment finds particular expression in the following areas:

EDUCATION scholarships and internships, support of university chairs.

HEALTH contributions to foundations, research institutes and other non-profit agencies.

CULTURE support of cultural and artistic development in the fields of theatre and music, most particularly as it relates to the next generation.

SOCIAL AND COMMUNITY CAUSES support of organizations working to improve living conditions in communities neighbouring the Partnership's facilities.

Gaz Métropolitain and its employees also contribute to major social and community causes through Centraide. In 2002, contributions to Centraide by the Partnership and its employees exceeded $160,000.

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Gaz Métropolitain has made **health** care one of its priorities.

## CONSTANT SUPPORT OF UNIVERSITY EDUCATION

Whether through the *Flamme Bleue* contest, which stimulates the creativity of students in the *Design de l'environnement* and *École de design* departments at *Université du Québec à Montréal*, or through the *Bourse Green–Gaz Métropolitain* program, which supports the efforts of post-graduate students in Economics at *Université Laval*, the Partnership encourages the development of the potential of Québec universities.

## SIGNIFICANT CONTRIBUTIONS TO HEALTH CARE

Aware of the most fundamental needs of Quebecers, Gaz Métropolitain has made health care one of its priorities. The Partnership contributes to many foundations and research institutes, including *La Maison des Greffés*, CHUQ, the Montréal Children's Hospital, as well as breast cancer research.

## EMPLOYEES WITH THE CHRISTMAS SPIRIT– ALL YEAR LONG!

Every year for more than 15 years, our employees have joined forces to collect funds for the distribution of Christmas baskets in the Hochelaga-Maisonneuve and Centre-South neighbourhoods of Montréal. The objective: to help needy families who live near the Partnership's headquarters celebrate Christmas. Over the past five years, more than $185,000 has been collected, and our volunteer employees have packed and personally delivered food baskets to more than 200 families in the neighbourhood.

## TAKING LOCAL SCHOOL CHILDREN UNDER OUR WING

Since 1996, Gaz Métropolitain has been taking a lively interest in the youngsters attending Hochelaga primary school, which is located near its headquarters building. A committee of volunteer employees, in concert with representatives from the school, determines the most pressing needs. This sponsorship helps make extra-curricular projects and sociocultural activities possible, or meets the need for clothes, snacks, lunches or school supplies. So it's not surprising that when the time came to replace its IT equipment, Gaz Métropolitain gave the school several computers. Gaz Métropolitain also welcomes the school children to its headquarters twice each year: once for Career Day and again for the Christmas Party organized especially for them.

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*Le Petit cirque Gaz Métro* has been introducing youngsters **aged 5-12** from the Hochelaga-Maisonneuve neighbourhood to the magic of the circus and the theatre since 2000.

## LE PETIT CIRQUE GAZ MÉTRO

*Le Petit cirque Gaz Métro* has been introducing youngsters aged 5-12 from the Hochelaga-Maisonneuve neighbourhood to the magic of the circus and the theatre since 2000. The children have a lot of fun trying out juggling, acrobatics and acting, while developing self-esteem and respect for others. At the end of either of the two 10-week sessions organized each year, participants in this community project can enjoy a week of recreation at the Jeune-Air camp in the Laurentians, at the *Centre de vacances et de plein air le P'tit bonheur.*

## SUPPORT FOR RELÈVE EN BLUES

In 2002, Gaz Métropolitain joined with *Festiblues International de Montréal* in offering new talent an opportunity to show what they can do before a large audience. The *Relève en blues Gaz Métropolitain* contest gave seven new groups of young musicians from different regions of Québec a chance to be discovered. The profits from this annual festival go to the *Fondation jeunesse Bordeaux-Cartierville.* Among other benefits, the event helps about a hundred youths from under-privileged districts learn about the job market, about responsibilities, and about working in a teamwork. Thanks to joint sponsorship with the Club Lion d'Or, contest winners had the opportunity to make an appearance on a professional stage that has seen many a star in its day.

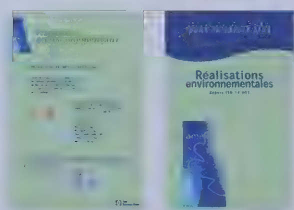
# ENVIRONMENT

## A RIGOROUS ENVIRONMENTAL MANAGEMENT SYSTEM

Gaz Métropolitain uses an environmental management system (EMS) in the operation of its distribution system. EMS helps identify the potential impacts on the environment of activities so they can be eliminated or mitigated. With its various tools that ensure sound environmental management and continuous improvement, EMS facilitates adherence to the Gaz Métropolitain environmental policy, which focuses on:

- Legal compliance and pollution prevention;
- Environmental protection;
- Energy efficiency and replacement of more polluting energies;
- Cooperation with the community.

Having obtained this international recognition,
**ISO 14001**
which took two years to achieve, the Partnership now has the challenge of maintaining the standard.




**EMS**
helps identify the potential impacts on the environment of activities so they can be eliminated or mitigated.

## CONCERN FOR THE QUALITY OF THE ENVIRONMENT

In adopting its environmental policy, Gaz Métropolitain undertook to show leadership, discipline and determination in continuing its efforts to safeguard the environment. Through its environmental management system, pollution prevention is integrated into the company's day-to-day activities.

Beyond strict compliance with the laws and regulations in effect, the environmental programs put in place have helped optimize the use of resources, decrease the amount of waste materials, reduce greenhouse gas emissions, and promote energy efficiency with customers.

## ENVIRONMENTAL MANAGEMENT THAT CONFORMS TO INTERNATIONAL STANDARDS

In October 2000, Gaz Métropolitain's environmental management system was registered under ISO 14001 (International Organization for Standardization) by the Québec Standards Bureau. Having obtained this international recognition, which took two years to achieve, the Partnership now has the challenge of maintaining the standard. As a result of the hard work and commitment of employees and managers, our certification has been extended at each of the audits conducted every six months by registered external auditors.

## NATURAL GAS TO SAFEGUARD THE ENVIRONMENT

Natural gas is an efficient and secure source of energy that helps safeguard the quality of the environment. The characteristics of natural gas make for its efficient use and offer greater potential for reducing polluting emissions than do other forms of fuel.

Of all the fossil fuels, natural gas is recognized for its effective contribution to reducing greenhouse gases and fighting smog and acid rain. Its growing use in a wide variety of ways, from residential heating to industrial cogeneration, is an immediate solution to current environmental problems.

The total reduction over eleven years corresponds to a reduction of

**30.8%**

per cubic metre delivered since 1990, and represents the equivalent of 23.3 kilotonnes of $CO_2$.

The EEP programs have generated energy savings equal to more than

**3.9 million**

cubic metres of natural gas since their introduction in November 2000.

## MITIGATING CLIMATE CHANGE

Gaz Métropolitain is raising the awareness of its employees, customers and partners to the importance of sound environmental management and of reducing greenhouse gas emissions. The Partnership has set a target to reduce the losses of natural gas from the operation of its system by 20% between 1990 and 2008. In 2001, and for the eleventh consecutive year, Gaz Métropolitain succeeded in reducing those losses, which become greenhouse gas emissions. The total reduction over eleven years corresponds to a reduction of 30.8% per cubic metre delivered since 1990, and represents the equivalent of 23.3 kilotonnes of $CO_2$.

## USING ENERGY MORE EFFICIENTLY

Gaz Métropolitain is also promoting energy efficiency with its customers. The various programs under the Energy Efficiency Plan (EEP) offer them tools to help them achieve savings while reducing greenhouse gas emissions. The programs have generated energy savings equal to more than 3.9 million cubic metres of natural gas since their introduction in November 2000. In the EEP 2002-2005 three-year plan, the energy savings forecast are equivalent to a reduction of 798 kilotonnes of $CO_2$ over the life of the measures.

# MD&A

## HIGHLIGHTS

In 2002, Partners' income was up by $13.4 million, or 9.5%, to a record $154.6 million ($1.40 per unit) compared to $141.2 million ($1.28 per unit) in 2001. This achievement is all the more remarkable because, as is explained further on, a reduction in the federal tax rate reduced Partners' income by approximately $4.0 million compared to 2001.

Partners' income was up over 2001 levels for each of the Partnership's three sectors of activity in 2002. Of the total increase, $7.5 million comes from the Distribution Sector and $2.5 million from the Transportation Sector. The Energy Services Sector succeeded in breaking even in its second full year as an independent business with a turnaround of $1.3 million.

## CONSOLIDATED OPERATING RESULTS

### REVENUES

Revenues are down by $462 million, or 22.3%, to $1.608 billion compared to $2.070 billion in 2001. The decrease can be explained primarily by lower system gas prices, which fell by 31.4 % from an average of $6.79/gigajoule in 2001 to $4.66/gigajoule in 2002. Natural gas purchased by the Partnership is billed at cost to customers in Québec, with the result that fluctuations in natural gas prices do not have any direct impact on gross margin or Partners' income.

### GROSS MARGIN

Gross margin is $555.9 million for the 2002 fiscal year compared to $537.1 million for the preceding year. The net increase of $18.8 million, or 3.5%, is basically due to the Partners' share of overearnings from the Québec distribution activity and the improved profitability of subsidiaries and other investment interests.

### EXPENSES

Operations and maintenance expenses of $176.7 million in 2002 are up by $9.2 million compared to $167.5 million the preceding year. The Québec distribution activity faced, among other things, a very substantial increase in the cost of insurance following the events of September 11, 2001 and also contributed to the pension fund following a contribution holiday in 2001. Depreciation and amortization of $135.2 million are $8.1 million higher than the preceding year, primarily on account of investments in the distribution systems over the past few years. Interest on long-term debt is down by $10.9 million to $84.5 million from $95.4 million in 2001, representing reductions in interest rates and in the debt load required to finance inventories and accounts receivable, which were also down due to lower gas prices. In addition, financial and other expenses, which represent interest on short-term debt, amount to $4.9 million compared to $5.9 million in 2001. Total expenses are up by $5.4 million from $395.9 million in 2001 to $401.3 million in 2002.

## PARTNERS' INCOME

Partners' income is up by $13.4 million to $154.6 million in 2002 compared to $141.2 million in 2001. Results for the 2002 year include the Partnership's $9.0 million share of the overearnings of $27.1 million from the Québec distribution activity for the 2002 year. The remaining $18.1 million will be distributed in the form of a $12.8 million reduction in customer rates and a $5.3 million contribution will be made to the Energy Efficiency Fund. Although there were no overearnings in 2001, an amount of $3.0 million had been recorded with respect to amounts earned in 2000. Since the introduction of the performance incentive mechanism on October 1, 2000, the Partnership's share of overearnings is recorded in the year earned.

Partners' income is approximately $4.0 million less than what it would have been if the federal corporate tax rate had remained the same as in 2001. The Partnership and TQM Pipeline and Company, Limited Partnership ("TQM") include a deemed current tax cost in the rates for their regulated activities. The 2% reduction in the federal tax rate in 2002 represents a decrease in revenues and Partners' income of approximately $4.0 million. Two additional decreases of 2% each in the federal tax rate will also affect Partners' income for the 2003 and 2004 years.

The average number of outstanding units of 110.5 million is the same as the preceding year. Partners' income per unit of $1.40 for the 2002 year is up by $0.12 from $1.28 in 2001.

## INCOME TAX

Because of the Partnership's limited partnership status, income tax is not included in the calculation of Partners' income; such expense is borne by each Partner. The Partnership has an agreement with the tax authorities on harmonizing as much as possible the rules for calculating income for tax purposes with regulatory accounting principles. For the year ended September 30, 2002, income for tax purposes exceeded distributions by 26.8% for federal purposes and 26.4% for Québec purposes. On average, since 1993, income for tax purposes has exceeded distributions by 7.4% for federal purposes and 6.6% for Québec purposes. Historically, differences have been as high as +26.8% (unfavourable difference for a taxable Partner) and a low of –18.1% (favourable variance for a taxable Partner). Partners that hold their units in a non-taxable vehicle, such as an RRSP, are not affected by the difference between income for tax purposes and distributions received.

## FINANCIAL STRUCTURE

The Partnership's balance sheet shows total assets of $2.350 billion in 2002, the same as the preceding year. The reduction in "Other" assets, i.e. deferred charges, goodwill and other investments, was offset by increases in net property, plant and equipment and current assets. The $17.8 million decrease in "Other" assets can be explained primarily by a decrease in deferred charges as a result of a reduction in system gas prices ($54.9 million), offset in part by an increase in the rate stabilization accounts ($34.8 million). The increase in property, plant and equipment is due to an $8.0 million increase in net investments to develop and improve the various transportation and distribution systems. The $10.0 million increase in current assets can essentially be explained by higher cash and trade receivables.

The accounts receivable securitization program optimizes the utilization of the Partnership's financial assets. A maximum limit of $85.0 million has been negotiated with a financial institution. As at September 30, 2002, the value of the accounts receivable that had been securitized and, therefore not shown in the balance sheet, net of the subordinated rights retained by the Partnership, amounts to $47.5 million compared to $63.0 at the end of the 2001 year.

Long-term debt includes first mortgage bonds issued by the Partnership and the pro rata share of those issued by TQM. These bonds bear interest at fixed rates and mature at various dates up to October 2030. As at September 30, 2002, total outstanding bonds amount to $853.5 million ($856.5 million in 2001). The Partnership's policy is to fix interest rates on approximately 75% of its long-term debt and leave the balance at floating rates. As at September 30, 2002, 76% of total long-term debt is at fixed rates.

The Partnership has various bank lines of credit, including a term loan of $300.0 million and operating lines totalling $193.0 million. The term loan can be used to finance the Partnership's current operations and capital expenditures or to support its commercial notes program. As at September 30, 2002, total borrowings on these lines, including the commercial notes, are $223.9 million ($234.6 million in 2001). No repayments of the term loan are required before April 30, 2005.

Subsidiaries and joint ventures have term loans and operating lines. The Partnership's pro rata share of these facilities is $168.0 million and $51.7 million respectively. As at September 30, 2002, the share of the borrowings from these facilities totals $185.0 million ($207.6 million in 2001).

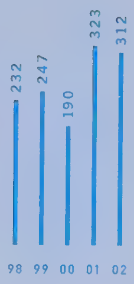
The operating lines of the Partnership, its subsidiaries and joint ventures are sufficient to meet seasonal cash flow requirements for the 2003 fiscal year.

Partners' equity of $822.7 million as at September 30, 2002 is $10.8 million higher than the preceding year. This can be explained by a $13.2 million excess of Partners' income over distributions paid, net of a $2.9 million goodwill write-off in respect of certain investments as a result of the adoption, effective October 1, 2001, of the new accounting standards relating to goodwill (Note 2 of Consolidated Financial Statements).

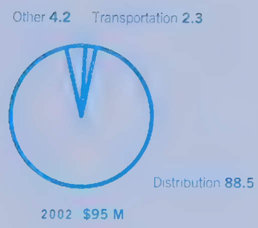
As indicated in the financial statements, the Partnership uses financial derivatives to stabilize the cost of natural gas. The Partnership had the new parameters of its derivatives policy approved by the *Régie de l'énergie* for the distribution of gas in Québec. This policy establishes the parameters for using financial instruments to protect customers against the volatility of system gas costs. On average, as at September 30, 2002, the cost of this partial protection is $0.07/ gigajoule for total forecast system gas volumes for the next three years. Moreover, gains or losses attributable to these financial instruments are reimbursed or recovered through gas supply rates in accordance with the method approved by the Régie.

In addition, the Partnership and certain subsidiaries and joint ventures use swaps to hedge against possible interest rate hikes or foreign exchange fluctuations. In line with the Partnership's policy, derivative products are only used to cover risks flowing from actual transactions and cannot be used for speculative purposes.

CASH FLOWS PROVIDED BY OPERATIONS
(IN MILLIONS OF DOLLARS)




ACQUISITIONS OF PROPERTY, PLANT & EQUIPMENT
(IN MILLIONS OF DOLLARS)




The Partnership's financial structure and stability have enabled it to obtain from Standard & Poors credit ratings of A for its long-term bonds and A-1 (low) for its commercial paper, as well as ratings of A and R-1 (low) from Dominion Bond Rating Service.

## LIQUIDITY AND CAPITAL STRUCTURE

Consolidated cash flows, before changes in non-cash working capital items, total $286.2 million compared to $297.5 million generated during the preceding year, a decrease of $11.3 million, or 3.8%. This decrease can be explained by the increase in the rate stabilization accounts, primarily the impact of temperatures for 2002.

The rate stabilization accounts normalizes revenues upward or downward based on volumes that would have been sold in Québec if temperatures had been normal. However, this does not involve any receipt or outlay of funds in the year volumes are normalized. Revenues were adjusted upward by $50.5 million in 2002, compared to $5.3 million in 2001. This can be explained by temperatures that were milder than normal and milder than in 2001. The regulatory mechanism provides that the Partnership may, starting in the second subsequent year, recover the adjustment in its rates over the next five fiscal years.

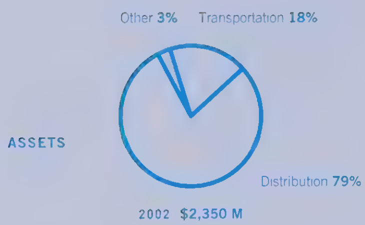
Non-cash working capital items generated $25.3 million compared to $25.6 million in 2001. There are two explanations for the lower cash receipts in 2002. Firstly, in 2001, natural gas prices had fallen during the year, resulting in a substantial decrease in trade and other receivables compared to 2000, thereby generating substantial cash flows. This did not recur in 2002. Secondly, accounts payable and accrued liabilities increased in 2002, which offset the decrease in cash flows related to trade and other receivables. Operating activities, after the change in non-cash working capital items, generated $311.6 million during the past fiscal year compared to $323.0 million in 2001.

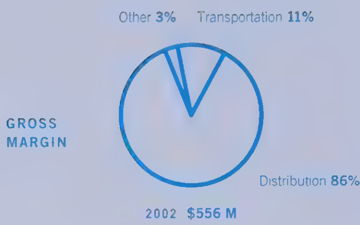
The Partnership made investments of $124.1 million in 2002 compared to $257.9 million in 2001, a decrease of $133.8 million. Deferred charges of $24.7 million are down by $147.4 million from the 2001 year. This significant reduction can be explained primarily by the decrease in deferred charges related to the cost of natural gas.

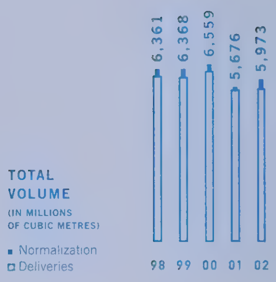
Acquisitions of property, plant and equipment are up by $14.2 million in 2002 to $95.0 million. This increase can be explained primarily by higher investments in Québec distribution activities.

Two transactions account substantially for the $1.9 million increase in goodwill during 2002. Gaz Métropolitain Plus Limited Partnership acquired 100% of Servitech Combustion inc. and increased its interest in Option Gaz Ltée from 50% to 100%.

Distributions to Partners in 2002 amount to $141.4 million compared to $140.3 million the preceding year. Distributions per unit total $1.28 in 2002, compared to $1.27 in 2001.




## ACTIVITIES BY SECTOR

The Partnership's three sectors of activity are the distribution and transportation of natural gas as well as energy services and other activities. The distribution of natural gas in Québec is the Partnership's core business. This sector includes the natural gas distribution activities of the Northern New England Gas Corporation ("NNEG") group in Vermont.

The transportation sector includes a 50% interest in TQM and a 20.7% interest in Portland Natural Gas Transmission System ("PNGTS"). It also includes the activities of Champion Pipe Line Corporation Ltd. ("Champion"), a subsidiary.

Energy services and other includes the Partnership's unregulated activities, in particular the activities of Gaz Métropolitain Plus Limited Partnership, and its wholly-owned subsidiaries such as Climatisation et Chauffage Urbains de Montréal, Servitech Combustion inc. and Option Gaz Ltée. Investment interests in Aqua Data inc./Stelem inc., Aqua-Rehab inc. Group, Systèmes Teldig inc. and Sofame Technologies inc. are also part of this sector.

The Partnership's assets consist mainly of property, plant and equipment used for the distribution of natural gas. Of total assets of $2.350 billion, 79% relate to the distribution sector, 18% to transportation activities and 3% to energy services and other, a breakdown which is similar to 2001.

The Partnership's distribution revenues include the cost of natural gas, which, as has already been explained, has no impact on the results of the Québec distribution activity, the core business. Accordingly, gross margin provides a better indication of the Partnership's performance than revenues. Distribution and transportation activities generate 97% of the gross margin of $556 million. The rates that generate this portion of the gross margin are set by regulatory bodies based on the approved cost of service, including a return on equity employed. Energy services and other generated 3% of the Partnership's consolidated gross margin in 2002.

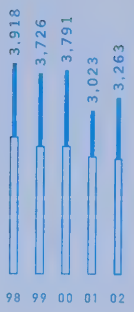
In 2002, the transportation and distribution sectors generated all of the Partners' income. Energy services and other broke even.

## DISTRIBUTION SECTOR

The Partnership delivers approximately 97% of the natural gas consumed in Québec. Vermont Gas Systems, Inc. ("VGS"), a wholly-owned subsidiary, is the sole gas distributor in Vermont. In 2002, deliveries in Vermont represented 4% of the Partnership's total deliveries.

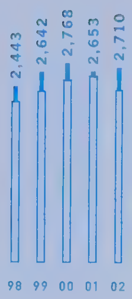
**DELIVERIES TO INDUSTRIAL CUSTOMERS**
(IN MILLIONS OF CUBIC METRES)

■ Interruptible service
□ Firm service

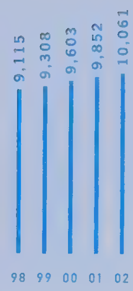



**DELIVERIES TO COMMERCIAL AND RESIDENTIAL CUSTOMERS**
(IN MILLIONS OF CUBIC METRES)

■ Normalization
□ Deliveries




**KILOMETRES OF DISTRIBUTION MAINS**



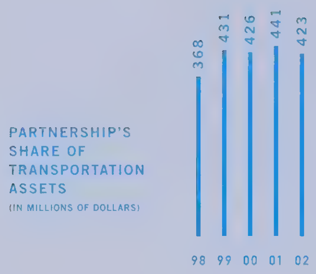

In Québec, the Partnership benefits from a normalization mechanism for its distribution revenues based on normal temperatures. Normalized volumes (for temperatures), which are more representative of the performance of the Partnership's core business, were up by 5.2% from 5,676 million cubic metres in 2001 to 5,973 million cubic metres in 2002. Temperatures have been milder than normal for the past two years and the normalization represented 293 million cubic metres in 2002 compared to 37 million in 2001.

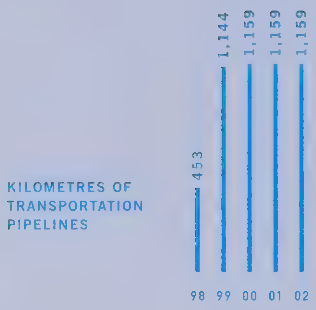
In the commercial and residential markets, normalized volumes were up by 57 million cubic metres, or 2.2%, from 2,653 million cubic metres in 2001 to 2,710 million cubic metres. In the industrial market, where the normalization mechanism does not apply, total deliveries are 3,263 million cubic metres in 2002, an increase of 7.9 % compared to 3,023 million cubic metres in 2001. Lower natural gas prices and milder temperatures, which translated into fewer interruptions, largely accounts for the increase in deliveries to customers on interruptible service.

In spite of milder temperatures, actual deliveries were up 0.7% in 2002 to 5,680 million cubic metres compared to 5,639 million cubic metres in 2001. The increase is attributable to higher deliveries in the industrial market, offset by a 7.6% decrease in deliveries in the commercial and residential markets, which dropped from 2,616 million cubic metres in 2001 to 2,417 million cubic metres in 2002.

Capital expenditures in the distribution sector totalled $88.5 million in 2002, compared to $73.9 million in 2001. Investments in 2002 included the construction of 209 kilometres of pipelines, system improvements, in particular in terms of safety, and various general expenditures, such as buildings and the vehicle fleet.

The distribution sector has 186,800 customers—152,600 in Québec and 34,200 in Vermont. To serve these customers, the Partnership had, as at September 30, 2002, 1,194 employees in Québec and 112 in Vermont. Operations and maintenance expenses for the distribution sector are $151.0 million in 2002, compared to $143.1 million in 2001, an increase of 5.5%. Depreciation and amortization amount to $113.7 million in 2002 compared to $107.8 million the preceding year. Interest on long-term debt is down from $70.4 million in 2001 to $65.0 million in 2002. This $5.4 million decrease can be explained by lower interest rates and the reduction in the debt load required to finance inventories and trade receivables, which are also down because of lower natural gas prices.




In conclusion, the distribution sector generated income of $142.1 million in 2002, compared to $134.6 million in 2001, an increase of $7.5 million.

## TRANSPORTATION SECTOR

The transportation sector includes the 50% investment in TQM, the 20.7% interest in PNGTS and the activities of Champion, a wholly-owned subsidiary. TQM operates a 572-kilometre transportation system in Québec that is composed of two lines—a line that extends from Saint-Lazare, west of the Island of Montréal, to Saint-Nicolas, in the suburbs of Québec City, and a line that extends from its mainline in Lachenaie to East Hereford, at the Québec/New Hampshire border. The 489-kilometre PNGTS pipeline originates at East Hereford and crosses parts of New Hampshire, Maine and Massachusetts to the suburbs of Boston. Champion serves the Partnership's distribution system in the Abitibi/Témiscamingue region in Québec with two gas pipelines totalling 98 kilometres.

TQM and Champion are regulated by the National Energy Board. TQM's cost of service is incorporated in the cost of service of TransCanada Pipelines to which TQM's system is connected. PNGTS is regulated by the Federal Energy Regulatory Commission ("FERC") in the United States. On October 1, 2001, PNGTS asked the FERC to approve an increase in its initial rates that were to be frozen until March 2002. The interested parties, i.e. PNGTS' customers, then had the regulatory proceedings suspended in order to negotiate a settlement with them. The FERC approved a provisional rate effective April 1, 2002. On October 25, 2002, the parties submitted an agreement to the FERC for approval.

For 2002, gross margin for the transportation sector is $62.8 million compared to $61.0 million in 2001. Operations and maintenance costs are $13.9 million in 2002 compared to $11.4 million in 2001. The increase is primarily due to the overall increase in insurance costs and expenses incurred in connection with the PNGTS rate review. Depreciation and amortization are $17.8 million in 2002 compared to $16.4 million in 2001. Interest on long-term debt of $18.2 million is down by $4.4 million from the 2001 year as a result of lower interest rates.

Partners' income generated by the transportation sector is therefore $12.8 million for the 2002 year compared to $10.3 million in 2001.

## ENERGY SERVICES AND OTHER

Revenues from unregulated activities are $56.0 million in 2002 compared to $48.0 million in 2001. The higher revenues reflect the growth in sales for Gaz Métropolitain Plus Limited Partnership, primarily as a result of its acquisition of Servitech Combustion inc. and the increase in its interest in Option Gaz Ltée. Gross margin of $18.0 million in 2002 is up $2.7 million over the 2001 year. Operations and maintenance expenses of $12.5 million are up $1.2 million over the preceding year due, among other things, to the two acquisitions in the year.

The Energy Services and Other sector, which had been restructured in 2001, improved its profitability by $1.3 million in 2002, thereby breaking even.

## SUBSEQUENT EVENT

Section 3870 of the Handbook of the Canadian Institute of Chartered Accountants ("CICA") entitled "Stock-based compensation and other stock-based payments" was published in December 2001. The standard defines a fair value-based accounting method that the Partnership will adopt ín 2003 for its Unit Option Plan. The adoption of the standard will not have a significant impact on the financial position or operating results of the Partnership.

## RISKS AND UNCERTAINTIES

As has already been stated, the Partnership's core business is the distribution of natural gas in its franchise areas in Québec and Vermont. Its ability to achieve sound financial results is mainly dependent on the competitiveness of natural gas in relation to other energy sources, the evolution of interest rates, the economic context in which the businesses it serves operate and the decisions rendered by regulatory bodies, in particular by the *Régie de l'énergie* with respect to rates and authorized return on Partners' equity allocated to Québec distribution. The base rate of return authorized by the *Régie de l'énergie* is determined by a formula that fixes the return as a function of forecast Canadian long-term interest rates. The base rate of return has been fixed at 9.89% for the 2003 year compared to 9.67% for 2002. It can be increased depending on forecast or realized productivity gains determined in accordance with the performance incentive mechanism approved by the Régie. The incentive is designed to reward the Partnership for generating a greater return on investments, optimizing asset use and exercising tighter control over costs. For 2003, the incentive included in rates represents 0.45%.

The Partnership's income growth over the longer term will depend in particular on the increase in investments related to the development of its distribution and transportation systems or the construction of gas pipelines or acquisitions. To a lesser extent, growth will also come from its ability to develop its unregulated activities.

At this point in time, the main concern with respect to the distribution activity is gas price levels over the medium term following the major fluctuations of the past two years. After peaking at $12.90/gigajoule in the 2001 winter, natural gas traded at an average of approximately $3.50 gigajoule during 2002. Natural gas prices are presently double 1998 levels and most medium-term forecasts indicate they will remain at this level.

Even though oil producers currently command a premium in the face of the threat of military action in Iraq, a major producer, light and heavy fuel oil prices are relatively attractive to certain users. In Québec, electricity has the greater share of the residential market and its stable price makes competition more difficult even if natural gas is almost on an even footing when modern high-performance appliances are used. In the commercial market, natural gas enjoys a generally favourable competitive position, which can be as great as 20% in certain segments.

If the difficult competitive situation in relation to heavy fuel oil were to persist, certain industrial customers and other large users might not be willing to make long-term commitments for significant volumes. However, there are considerations other than price that are also a factor when choosing an energy source. Ease of use, consumption-based billing and respect for the environment are characteristics that make natural gas a preferred choice.

In the transportation sector, improvement in the financial performance of PNGTS is subject to obtaining new rates that take account of gas pipeline construction costs and a reasonable rate of return as well as the settlement of certain litigation. Bringing these issues to a successful conclusion will make it possible for PNGTS to refinance its debt, as planned, in a favourable context.

The Partnership is moving ahead with its implementation of the Enterprise Resource Planning system that uses SAP technologies for all administrative functions in the Québec distribution activity. Phase II of the project, which covers customer relations and billings, will require significant resources and investments. The scope of the project involves business risks normally associated with the implementation of this type of system. At this point in time, management does not foresee any major issues.

## OUTLOOK AND PRIORITIES FOR THE 2003 FISCAL YEAR

The challenge for the current and future years will be to continue the profitable development of the distribution activity in Québec based on increasing the customer base in the commercial and residential markets, exercising tight control over expenses and ensuring the safety and reliability of the system. Financial performance is heavily dependent on the state of the economy and the demand for natural gas. To improve service quality and increase productivity in the Québec distribution activity, the Partnership is counting on the gradual implementation of blue-collar worker versatility in accordance with the terms of the new collective agreement negotiated in 2002. In Vermont, where gas is much less expensive than electricity and the competition comes from fuel oil, VGS anticipates continued development.

The Partnership does not foresee any major issues in the transportation sector over the next few years. In fact, results should be positively affected if the new PNGTS rates are approved. In the energy services sector, Gaz Métropolitain Plus will continue to improve profitability through the consolidation of its activities and increasing its sales. The other unregulated activities, in particular those centred on the diagnostics and rehabilitation of water and waste water systems, should continue to seize an increasing number of business opportunities arising from municipal infrastructure rehabilitation programs in Canada and the United States.

CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED SEPTEMBER 30, 2002 AND 2001

# FINANCIAL STATEMENTS

## MANAGEMENT'S REPORT

ON THE CONSOLIDATED FINANCIAL STATEMENTS OF GAZ MÉTROPOLITAIN AND COMPANY, LIMITED PARTNERSHIP

The consolidated financial statements of Gaz Métropolitain and Company, Limited Partnership and all of the information in this report are the responsibility of the management of Gaz Métropolitain, inc., acting in its capacity as General Partner of Gaz Métropolitain and Company, Limited Partnership. It is management's responsibility to select the appropriate accounting policies and to exercise its best judgement in determining reasonable and fair estimates based on Canadian generally accepted accounting principles and decisions from the Régie de l'énergie with respect to the natural gas distribution activity in Québec. Financial information found elsewhere in this report is consistent with the consolidated financial statements. This information and the consolidated financial statements are published with the Board of Directors' approval.

Management maintains accounting and internal control systems that are designed to provide reasonable assurance that accounting records are reliable and assets are safeguarded.

The Board of Directors assumes its responsibilities for the financial statements primarily through the Audit Committee, made up solely of outside directors. The Audit Committee has reviewed all of the information in this report as well as the annual financial statements and has recommended they be approved by the Board. The Audit Committee also examines on a continuous basis the quarterly financial results, the results of internal and external audits of accounting methods and the system of internal controls. The Audit Committee also recommends to the Board the choice of external auditors. The external and internal auditors are free to communicate with the Audit Committee.

The firm of Raymond Chabot Grant Thornton, Chartered Accountants, has been given the mandate to audit the consolidated financial statements of Gaz Métropolitain and Company, Limited Partnership in accordance with Canadian generally accepted auditing standards. Their audit included the tests and other procedures they deemed necessary under the circumstances. Their independent opinion on the financial statements is presented hereinafter.

**ROBERT TESSIER**
President and Chief Executive Officer
Gaz Métropolitain, inc.

**LUC SICOTTE**
Vice President and Chief Financial Officer
Gaz Métropolitain, inc.

Montréal, Canada
November 15, 2002

## AUDITORS' REPORT

TO THE PARTNERS OF GAZ MÉTROPOLITAIN AND COMPANY, LIMITED PARTNERSHIP

We have audited the consolidated balance sheets of Gaz Métropolitain and Company, Limited Partnership as at September 30, 2002 and 2001, and the consolidated statements of income, Partners' equity and consolidated cash flows for the years then ended. These financial statements are the responsibility of the management of Gaz Métropolitain, inc., acting in its capacity as General Partner of the Partnership. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Partnership as at September 30, 2002 and 2001, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Raymond Chabot Grant Thornton

**RAYMOND CHABOT GRANT THORNTON**
General Partnership
Chartered Accountants

Montréal, Canada
November 15, 2002

| Years ended September 30, (in thousands of dollars and thousands of units) | **2002** | 2001 |
|---|---|---|
| **REVENUES** | **$1,607,700** | $2,069,977 |
| **DIRECT COSTS** | **1,051,828** | 1,532,916 |
| **GROSS MARGIN** | **555,872** | 537,061 |
| **EXPENSES** | | |
| Operations and maintenance | **176,669** | 167,500 |
| Depreciation and amortization (Notes 4 and 5) | **135,211** | 127,111 |
| Interest on long-term debt | **84,513** | 95,430 |
| Financial and other | **4,899** | 5,856 |
| | **401,292** | 395,897 |
| **PARTNERS' INCOME** | **$ 154,580** | $ 141,164 |
| **BASIC AND DILUTED PARTNERS' INCOME PER UNIT** (in dollars) | **$ 1.40** | $ 1.28 |
| **WEIGHTED AVERAGE NUMBER OF OUTSTANDING UNITS** (Note 10) | | |
| Basic | **110,469** | 110,469 |
| Diluted | **110,473** | 110,469 |

The accompanying notes to the consolidated financial statements are an integral part of these statements.

## CONSOLIDATED PARTNERS' EQUITY

| Years ended September 30, (in thousands of dollars) | **2002** | 2001 |
|---|---|---|
| **CAPITAL** | | |
| Balance, beginning of year | **$799,250** | $798,381 |
| Cumulative effect of accounting change with respect to goodwill (Note 2) | **(2,919)** | – |
| Adjusted balance, beginning of year | **796,331** | 798,381 |
| Partners' income | **154,580** | 141,164 |
| | **950,911** | 939,545 |
| Distributions to Partners (Note 10) | **(141,400)** | (140,295) |
| Balance, end of year | **809,511** | 799,250 |
| **TRANSLATION ADJUSTMENT** | | |
| Balance, beginning of year | **12,595** | 7,579 |
| Change | **549** | 5,016 |
| Balance, end of year | **13,144** | 12,595 |
| **PARTNERS' EQUITY** | **$822,655** | $811,845 |

The accompanying notes to the consolidated financial statements are an integral part of these statements.

# CONSOLIDATED BALANCE SHEETS

| As at September 30, (in thousands of dollars) | 2002 | 2001 |
|---|---|---|
| **ASSETS** | | |
| CURRENT ASSETS | | |
| Cash | **$ 10,640** | $ 3,708 |
| Trade and other receivables (Note 3) | **35,874** | 32,757 |
| Inventories | **216,343** | 216,534 |
| Prepaid expenses | **6,521** | 6,377 |
| | **269,378** | 259,376 |
| PROPERTY, PLANT AND EQUIPMENT (Note 4) | **1,758,678** | 1,750,700 |
| OTHER ITEMS | | |
| Deferred charges (Note 5) | **274,720** | 292,833 |
| Goodwill (Note 2) | **23,063** | 24,002 |
| Other investments (Note 6) | **24,049** | 22,785 |
| | **321,832** | 339,620 |
| | **$2,349,888** | $2,349,696 |
| **LIABILITIES** | | |
| CURRENT LIABILITIES | | |
| Bank borrowings (Note 8) | **$ 29,906** | $ 38,441 |
| Accounts payable and accrued liabilities | **256,216** | 229,086 |
| Debt maturing within one year | **44,351** | 3,099 |
| | **330,473** | 270,626 |
| LONG-TERM DEBT (Note 9) | **1,196,760** | 1,267,225 |
| | **1,527,233** | 1,537,851 |
| **PARTNERS' EQUITY** (Note 10) | **822,655** | 811,845 |
| | **$2,349,888** | $2,349,696 |

The accompanying notes to the consolidated financial statements are an integral part of these statements.

On behalf of the Board of Directors of Gaz Métropolitain, inc.,
in its capacity as General Partner

**ROBERT TESSIER**
Director

**RÉAL SUREAU**
Director

| Years ended September 30, (in thousands of dollars) | **2002** | 2001 |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Partners' income | **$ 154,580** | $ 141,164 |
| Non-cash items: | | |
| Depreciation of property, plant and equipment | **88,677** | 82,741 |
| Amortization of deferred charges and issue expenses | **47,670** | 44,374 |
| Amortization of goodwill | **–** | 1 172 |
| Reduction in deferred charges related to cost of natural gas | **45,801** | 32,329 |
| Rate stabilization accounts | **(50,491)** | (5,274) |
| Non-controlling interest and other | **–** | 953 |
| | **286,237** | 297,459 |
| Change in non-cash working capital items (Note 11a) | **25,330** | 25,559 |
| Cash flows related to operating activities | **311,567** | 323,018 |
| **INVESTING ACTIVITIES** | | |
| Purchases of property, plant and equipment | **(94,955)** | (80,833) |
| Deferred charges | **(24,718)** | (172,070) |
| Other investments | **(2,469)** | (4,974) |
| Goodwill | **(1,921)** | (16) |
| Cash flows related to investing activities | **(124,063)** | (257,893) |
| **FINANCING ACTIVITIES** | | |
| Change in bank borrowings | **(8,978)** | 4,536 |
| Change in term loan | **(9,138)** | (50,938) |
| Other long-term debt: | | |
| Issue | **14** | 125,139 |
| Repayments | **(21,070)** | (4,799) |
| Non-controlling interest | **–** | 859 |
| Distributions to Partners | **(141,400)** | (140,295) |
| Cash flows related to financing activities | **(180,572)** | (65,498) |
| **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** | **6,932** | (373) |
| **CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR** | **3,708** | 4,081 |
| **CASH AND CASH EQUIVALENTS, END OF YEAR** | **$ 10,640** | $ 3,708 |

The accompanying notes to the consolidated financial statements are an integral part of these statements.

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Gaz Métropolitain and Company, Limited Partnership (hereinafter the "Partnership" or "GMCLP") are prepared in accordance with Canadian generally accepted accounting principles. In preparing the consolidated financial statements, the Partnership's management has to make estimates and assumptions that have an impact on the assets and liabilities shown in the balance sheet, the contingent liabilities noted as at the date of the financial statements and on the revenues and expenses presented in the statement of income for the year. Actual results may differ from these estimates.

### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements of the Partnership include the accounts of GMCLP and its subsidiaries. In addition, the investments in joint ventures are accounted for under the proportionate consolidation method. Other investments are recorded at cost.

### REGULATION

GMCLP is engaged primarily in the distribution of natural gas by pipeline in Québec. This activity (hereinafter "GMCLP-QDA") is regulated and distribution rates are fixed by the Régie de l'énergie (hereinafter the "Régie") and the system development and marketing activities are subject to its supervision and control.

The Act respecting the Régie de l'énergie provides that the natural gas supply rate must reflect the actual acquisition cost of the distributor as well as any other supply condition allowed by suppliers. In Decision D-95-44, the Régie approved a periodic adjustment mechanism to the price of gas. In Decision D-90-42, the Régie approved an automatic rate adjustment mechanism, upward or downward as necessary, that allows the distributor to reflect cost variations arising from changes to the rates of its transportation and storage service suppliers and to the cost of compression gas.

The Act respecting the Régie de l'énergie also provides that distribution rates are set to enable the distributor to recover the cost of providing the service, to obtain a reasonable return on the rate base recognized by the Régie and to improve its performance by providing incentives.

In decision D-90-75 issued on December 19, 1990, as part of the corporate reorganization of August 12, 1991, the Régie determined that the rate of return on the rate base would be set using an "adjusted" capital structure. With this structure, Partners' equity allocated to the Québec distribution activity is in the order of 46.0%, including 38.5% that is compensated on the same basis as corporate common shares and 7.5% on the same basis as preferred shares. For regulatory purposes, GMCLP-QDA's operating expenses include deemed current income taxes, large corporations tax and capital tax. These deemed taxes are calculated as if GMCLP was a taxable Canadian corporation, notwithstanding the tax status and the tax rate of the Partners.

In addition, the Régie, in exercising its powers, renders decisions with respect to the use by GMCLP-QDA of certain accounting practices which differ from those otherwise applied in unregulated businesses, in particular with respect to certain deferred charges including rate stabilization accounts, property, plant and equipment and their related depreciation, income taxes and employee future benefits.

Certain activities of subsidiaries and joint ventures are regulated by bodies such as the *National Energy Board* (hereinafter "NEB"), the *Federal Energy Regulatory Commission* and the *Vermont Public Service Board*.

### CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash and very liquid short-term investments with a maturity of three months or less when purchased.

### INVENTORIES

Natural gas in storage is carried at average cost using the monthly adjustment method, approved by the Régie, which provides for the total cost to be charged to customers. Inventories of materials and supplies are carried at the lower of average cost and replacement value.

### PROPERTY, PLANT AND EQUIPMENT

Acquisitions, replacements and improvements are recorded at cost, including direct costs, general and administrative expenses and an allowance on funds used for certain construction projects as accepted by regulatory authorities. The historical cost of retired properties related to the distribution system and the retirement costs are applied against accumulated depreciation when the properties are retired. Under this method, no gain or loss on disposal of assets is realized.

Depreciation is calculated using mainly the straight-line method based on the residual useful lives of the existing assets. The rates are periodically revised and approved by the Régie and include recovery of the unamortized cost of existing assets, estimates of the future costs of retiring the properties and the profit and loss upon disposal of properties already retired.

### DEFERRED CHARGES

GMCLP defers certain charges that are amortized and recovered in its rates over various periods not exceeding ten years depending on the nature of such charges.

To alleviate the effect of unpredictable and uncontrollable factors on its operations, the principal one being the impact of temperature fluctuations on its revenues, GMCLP-QDA is authorized by the Régie to maintain various rate stabilization accounts. Beginning in the second subsequent year, annual fluctuations are amortized over five years and recovered in rates.

### GOODWILL

Goodwill represents the excess of the cost over the net amount of the values assigned to the assets acquired and liabilities assumed when an enterprise is acquired. Goodwill is subject to an annual impairment test. Such tests are also performed if events have occurred or circumstances changed indicating that there may be an impairment loss. The impairment test compares the carrying amount and the fair value of the Partnership's reporting units. If the carrying amount of a reporting unit is greater than its fair value, amortization of goodwill is measured on the basis of the excess of the carrying amount of goodwill over its fair value. The fair value of a reporting unit is calculated based on discounted cash flows or external valuations.

### DEVELOPMENT ACTIVITIES

The costs related to development activities are capitalized except in cases where GMCLP does not have reasonable assurance that these costs will be recovered in the future.

### FOREIGN CURRENCY TRANSLATION

Long-term debt payable in foreign currency is translated into Canadian dollars at the rate of exchange prevailing at year-end or, as the case may be, at rates prescribed in forward exchange contracts used for hedging purposes. Gains and losses arising from translation are included in the results for the current year.

The assets and liabilities of foreign subsidiaries that are self-sustaining with respect to financing and operations are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet date. Revenues and expenses are translated at the average rate prevailing during the fiscal year. Gains and losses are shown under the caption "Translation adjustment" in the consolidated Partners' equity.

### REVENUES

Revenues include estimated volumes delivered but not billed at the end of the year as well as the impact of rate stabilization accounts of GMCLP-QDA resulting from temperature fluctuations. GMCLP-QDA customers' share, including the amounts transferred to the Energy Efficiency Fund, of any overearnings is deducted from revenues.

### INCOME TAXES

GMCLP as well as its subsidiaries and joint ventures formed as limited partnerships do not show income tax expense since under existing legislation, it is the Partners who are taxable.

Subsidiaries and joint ventures formed as corporations use the tax liability method to record income taxes, with the exception of one subsidiary that uses the taxes payable method, as authorized by the NEB.

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

### EMPLOYEE FUTURE BENEFITS

GMCLP-QDA charges pension contributions and post-employment benefits to income as the amounts are disbursed in accordance with the most probable assumptions with respect to the forecast return on the plan's assets, salary increases and retirement age.

GMCLP's subsidiaries and joint ventures record post-employment benefits in accordance with the accounting practices prescribed by the Canadian Institute of Chartered Accountants (hereinafter "CICA"). The pension contribution of defined contribution plans corresponds to the amount of the contributions made. The cost for defined benefit plans and other post-employment benefits is determined by actuarial calculation based on a projected benefit method prorated according to eligible years of service and is expensed as the services are rendered by the employees.

### UNIT-BASED COMPENSATION

GMCLP offers a unit option plan to named executives. No expense is charged to income when unit options are granted to these employees. The consideration received from the employees when they exercise the options will be credited to capital.

### INCOME PER UNIT

Income per unit is calculated on the basis of the weighted average number of outstanding units each year. The treasury stock method is used to determine the dilutive effect of unit options.

## 2. CHANGES IN ACCOUNTING POLICIES

### 2002

### A) INCOME PER UNIT

On October 1, 2001, the Partnership adopted retroactively the new recommendations of the CICA in Section 3500 of the CICA Handbook (hereinafter the "Handbook"), *Earnings per share*. Based on the new recommendations, the treasury stock (unit redemption) method, rather than the theoretical earnings method, should be used to determine the dilutive effect of outstanding unit options. The adoption of these recommendations has no effect on basic and diluted income per unit for the 2002 and 2001 years.

### B) FOREIGN CURRENCY TRANSLATION

On October 1, 2001, the Partnership adopted retroactively the new recommendations of the CICA in Section 1650 of the Handbook, *Foreign currency translation*, to discontinue the deferral and amortization of unrealized exchange gains and losses on foreign currency monetary items. Consequently, exchange gains or losses arising from translation are included in income for the year. The impact of these changes on the results for 2002 and 2001 is negligible.

### C) BUSINESS COMBINATIONS, GOODWILL AND OTHER INTANGIBLE ASSETS

In August 2001, the CICA issued Section 1581 of the Handbook, *Business combinations*, and Section 3062 of the Handbook, *Goodwill and other intangible assets*. The Partnership adopted the recommendations in these new sections, which are applicable to business combinations subsequent to June 30, 2001. The new standards require business combinations to be recorded using the new purchase method. In addition, intangible assets other than goodwill should be recorded separately if they meet the new criteria in the recommendations.

In addition, Section 3062 of the Handbook requires that goodwill and other tangible assets having an indefinite useful life not be amortized and that other identifiable intangible assets be amortized. Pursuant to these recommendations, GMCLP discontinued amortizing goodwill on October 1, 2001. As recommended, GMCLP performed transitional impairment tests of goodwill as of October 1, 2001, which resulted in the recognition of an impairment loss of $2,919,000. This loss was recorded as a change in accounting policy and applied to reduce opening Partners' equity for the year ending September 30, 2002.

For comparative purposes, the following table shows the effect on income if goodwill had not been amortized in 2001.

| | **2002** | 2001 |
|---|---|---|
| Partners' income | | |
| Partners' income per Statement of Income | **$154,580** | $141,164 |
| Amortization of goodwill | – | 1,172 |
| Adjusted Partners' income | **$154,580** | $142,336 |
| Basic and diluted income per unit (in dollars) | | |
| Basic and diluted income per unit per Statement of Income | **$ 1.40** | $ 1.28 |
| Amortization of goodwill | – | 0.01 |
| Adjusted basic and diluted income | **$ 1.40** | $ 1.29 |

**D) TRANSFERS OF RECEIVABLES**

On October 1, 2001, the Partnership adopted the new accounting guideline AcG-12, *Transfers of receivables,* which deals with the accounting requirements of the CICA relating to the transfer and servicing of receivables. In accordance with the provisions of AcG-12, the Partnership continued to report on its Agreement for the Acquisition and Transfer of Receivables signed in September 1996 based on preceding accounting instructions until September 30, 2001. On October 1, 2001, the agreement was cancelled and replaced by a new agreement whereby the Partnership transferred trade receivables to a securitization trust. These receivables are recorded as a transfer of receivables as the Partnership transfers control thereof and receives the related cash receipts from the trust. The adoption of these recommendations had no impact on the financial statements of the Partnership.

**2001**

**A) EMPLOYEE FUTURE BENEFITS**

As at October 1, 2000, certain subsidiaries and joint ventures adopted prospectively the new recommendations of the CICA in Section 3461 of the Handbook, *Future benefits.* The new standard requires the accrual basis of accounting for all employee future benefits – both pension and other post-employment benefits. Previously, these items were expensed as amounts were disbursed. The impact of adopting these new standards did not have a material effect on the Partnership's financial statements.

**B) FUTURE INCOME TAXES**

As at October 1, 2000, the Partnership adopted the new recommendations of the CICA in Section 3465 of the Handbook, *Future income taxes.* The new standards require that the amount of these future income taxes, and the taxes related to GMCLP's ownership interest in TQM relating to the regulated activities and not recognized by the Partnership, be calculated in accordance with the balance sheet method. Under this method, future income taxes are determined based on the difference between the accounting and tax bases of assets and liabilities. The future income tax assets and liabilities are calculated at the tax rate for a taxable Canadian corporation that should be in effect during the year the temporary differences should be realized or settled. In prior years, these amounts were calculated using the deferral method at the rate applicable to each of the fiscal years during which the differences had been created and were not adjusted for the current rate. The cumulative effect of the change from the deferral method to the balance sheet method in Section 3465 of the Handbook on this net future income tax liability amounts to $24,737,000 receivable as at October 1, 2000.

**EFFECTIVE IN 2003**

**A) STOCK-BASED COMPENSATION AND OTHER STOCK-BASED PAYMENTS**

On December 31, 2001, the CICA issued Section 3870 of the Handbook, *Stock-based compensation and other stock-based payments,* which applies to fiscal years starting on or after January 1, 2002. Among other things, the Section sets down the recognition, measurement and reporting standards for stock-based compensation and other stock-based payments. It recommends a recognition method based on fair value and encourages enterprises to adopt it for their stock-based compensation programs. Under this method, the compensation cost should be measured at the date of attribution based on the fair value of the attribution and should be recognized over the period of service. The Partnership will adopt this method, effective October 1, 2002, and does not expect that the adoption of the standard will have a significant impact on its financial position or operating results.

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 3. TRADE AND OTHER RECEIVABLES

### TRANSFER OF RECEIVABLES

On October 1, 2001, the Partnership signed an agreement for the regular transfer of receivables to a securitization trust. Receivables transferred in excess of amounts received in cash represent the subordinated rights retained by the Partnership that are included in Trade and other receivables in the balance sheet.

The securitization trust has no recourse against the other assets of the Partnership in the event debtors fail to pay amounts owing when they become due. GMCLP retained responsibility for the management, administration and collection of the receivables sold. No asset or liability with respect to the management of the receivables has been recorded given that the monetary benefits that GMCLP derives in this regard is almost equal to the value of the services provided.

The expense recorded in respect of the sale of receivables is $1,721,000 in 2002 and $2,393,000 in 2001.

As at September 30, 2002, the amount of the receivables transferred, net of the subordinated rights retained by the Partnership, amounts to $47,500,000 ($63,000,000 as at September 30, 2001). Under the new agreement, the maximum authorized is $85,000,000, compared to $100,000,000 under the preceding agreement, which expired on October 1, 2001.

The net cash consideration received (paid) relating to the transfer and sale of receivables of ($15,500,000) in 2002 and $20,000,000 in 2001 has been presented as a change in Trade and other receivables in the Consolidated Statement of Cash Flows.

## 4. PROPERTY, PLANT AND EQUIPMENT

| | | | 2002 | | | 2001 |
|---|---|---|---|---|---|---|
| | Cost | Accumulated depreciation | Net book value | Cost | Accumulated depreciation | Net book value |
| Storage | **$ 26,480** | **$ 13,045** | **$ 13,435** | $ 24,510 | $ 12,360 | $ 12,150 |
| Transportation | **845,878** | **362,688** | **483,190** | 852,453 | 340,013 | 512,440 |
| Distribution | **1,998,784** | **655,367** | **1,343,417** | 1,943,046 | 605,236 | 1,337,810 |
| General plant | **208,626** | **87,500** | **121,126** | 180,363 | 73,221 | 107,142 |
| | **3,079,768** | **1,118,600** | **1,961,168** | 3,000,372 | 1,030,830 | 1,969,542 |
| Government grants | **(443,494)** | **(241,004)** | **(202,490)** | (444,152) | (225,310) | (218,842) |
| | **$2,636,274** | **$ 877,596** | **$1,758,678** | $2,556,220 | $ 805,520 | $1,750,700 |

Average depreciation rates are 3.47% in 2002 and 3.36% in 2001. Depreciation is $88,677,000 in 2002 and $82,741,000 in 2001.

## 5. DEFERRED CHARGES

| | 2002 | 2001 |
|---|---|---|
| Conversion grants | **$ 61,661** | $ 57,187 |
| Costs related to infrastructure projects | **7,699** | 11,548 |
| Development of information technology | **49,585** | 38,900 |
| Rate flexibility | **1,293** | 1,844 |
| Long-term debt issue expenses | **7,604** | 9,932 |
| Expenses related to natural gas costs | **26,937** | 81,871 |
| Rate stabilization accounts | **105,621** | 70,795 |
| Other | **14,320** | 20,756 |
| | **$274,720** | $292,833 |

Amortization of deferred charges is $46,534,000 in 2002 and $43,198,000 in 2001, and the amortization of long-term debt issue expenses included in interest on long-term debt is $1,136,000 in 2002 and $1,176,000 in 2001. The reduction in deferred charges related to natural gas costs, including transportation and storage, is $45,801,000 in 2002 and $32,329,000 in 2001.

## 6. OTHER INVESTMENTS

| | 2002 | 2001 |
|---|---|---|
| Shares and debentures - Cable VDN inc., | **$15,565** | $12,834 |
| Preferred shares of a subsidiary of Gaz Métropolitain, inc. (Notes 9i and 16) | **7,396** | 7,396 |
| Loans to customers and other | **1,088** | 2,555 |
| | **$24,049** | $22,785 |

## 7. INTEREST IN JOINT VENTURES

| | 2002 | 2001 |
|---|---|---|
| **OWNED BY GMCLP** | | |
| TQM Pipeline and Company, Limited Partnership ("TQM"): | **50.0%** | 50.0% |
| Aqua-Rehab Group Inc.: | **50.0%** | 50.0% |
| Sofame Technologies Inc.: | **37.3%** | 34.5% |
| 3632491 Canada Inc. (sole shareholder of Aqua Data Inc. and Stelem Inc.): | **50.0%** | 50.0% |
| TelDig Systems Inc.; | **50.0%** | 50.0% |
| **OWNED THROUGH SUBSIDIARIES** | | |
| Portland Natural Gas Transmission System ("PNGTS"): | **20.7%** | 20.7% |
| Option Gaz Ltée (1): | **–** | 50.0% |

GMCLP's share of the consolidated financial statement components of the joint ventures is as follows:

| | 2002 | 2001 |
|---|---|---|
| **INCOME** | | |
| Revenues | **$ 71,091** | $ 67,601 |
| Expenses, | **60,280** | 53,723 |
| Net income | **$ 10,811** | $ 13,878 |
| **BALANCE SHEET** | | |
| Current assets | **$ 26,164** | $ 24,862 |
| Long-term assets | **398,753** | 412,802 |
| | **$424,917** | $437,664 |
| Current liabilities | **$ 57,867** | $ 26,738 |
| Long-term liabilities | **226,742** | 268,710 |
| | **284,609** | 295,448 |
| Partners' equity | **140,308** | 142,216 |
| | **$424,917** | $437,664 |
| **CASH FLOWS RELATED TO:** | | |
| Operating activities | **$ 16,256** | $ 25,833 |
| Investing activities | **(4,073)** | (5,063) |
| Financing activities | **(14,686)** | (19,462) |
| Increase in cash and cash equivalents | **$ (2,503)** | $ 1,308 |

(1) Since June 2002, Option Gaz Ltée has been wholly owned by a subsidiary of GMCLP.

## 8. BANK BORROWINGS

The short-term bank borrowings and credit lines of GMCLP and its TQM joint venture are unsecured and bear interest at a rate of 2.90% and 4.50% respectively as at September 30, 2002, and of 3.65% and 4.30% respectively as at September 30, 2001. The maximum authorized amounts for these borrowings are $193,000,000 for GMCLP and $25,000,000 for its share in TQM.

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 8. BANK BORROWINGS (CONT'D)

As at September 30, 2002 and 2001, bank loans and credit lines of Vermont Gas Systems (hereinafter "VGS") bear interest at the rate of 1.85% and 3.04% respectively. The maximum authorized loan of $19,046,000 (US$12,000,000) for VGS is unsecured.

## 9. LONG-TERM DEBT

| | Interest rate | Year of maturity | 2002 | 2001 |
|---|---|---|---|---|
| **GMCLP** (a) | | | | |
| First mortgage bonds (b) | | | | |
| Series | 11.75% | 2006 | $ 36,000 | $ 39,000 |
| Series | 10.75% | 2007 | 75,000 | 75,000 |
| Series "D" | 10.45% | 2017 | 125,000 | 125,000 |
| Series "E" | 9.00% | 2025 | 100,000 | 100,000 |
| Series "F" | 7.20% | 2028 | 50,000 | 50,000 |
| Series "H" | 6.05% | 2009 | 100,000 | 100,000 |
| Series "H" | 6.95% | 2010 | 100,000 | 100,000 |
| Series "I" | 7.05% | 2031 | 125,000 | 125,000 |
| | | | 711,000 | 714,000 |
| Term loan (3.94% in 2001) (c) | 2.96% | 2005 | 216,447 | 223,601 |
| Other (5.66% in 2001) | 5.74% | 2005 | 1,181 | 2,744 |
| | | | 928,628 | 940,345 |
| **NNEG** | | | | |
| Term note NNEG (d) (US$10,200 in 2001) | | | – | 16,101 |
| Unsecured preferred note of VGS (US$10,000 in 2002 and 2001) | 7.62% | 2028 | 15,872 | 15,785 |
| PNGTS term loan (6.22% in 2001) (e) (US$52,910 in 2002 and 2001) | 5.38% | 2003 | 83,979 | 83,519 |
| | | | 99,851 | 115 405 |
| **TQM** | | | | |
| First mortgage bonds (f) | | | | |
| Series "G" | 8.51% | 2005 | 42,500 | 42,500 |
| Series "H" | 6.50% | 2009 | 50,000 | 50,000 |
| Series "I" | 7.05% | 2010 | 50,000 | 50,000 |
| | | | 142,500 | 142,500 |
| Term loan (4.18% in 2001) (g) | 3.16% | 2003 | 40,350 | 42,350 |
| | | | 182,850 | 184,850 |
| **OTHER** | | | | |
| Non-recourse term loans and other (4.26% in 2001) (h) | 3.59% | 2003 to 2007 | 22,416 | 22,358 |
| Preferred units (i) | | | 7,366 | 7,366 |
| | | | 29,782 | 29,724 |
| | | | 1,241,111 | 1,270,324 |
| **CURRENT PORTIONS** | | | 44,351 | 3,099 |
| | | | $1,196,760 | $1,267,225 |

### ANNUAL CAPITAL REPAYMENTS:

Annual capital repayments required during the next five years to meet maturities and sinking fund requirements, excluding redemptions before maturity at GMCLP's option are:

2003: $44,351,000
2004: $11,087,000
2005: $262,020,000
2006: $27,025,000
2007: $88,049,000

a) The first mortgage bonds and the term loan are secured under a trust deed which contains a hypothec on the universality of movable property, present and future, of GMCLP situated in the province of Québec. These loans are also covered by a first immovable hypothec on the GMCLP present and future pipelines and gas system.

b) GMCLP's first mortgage bonds are redeemable at the greater of the face value or the value that reflects market conditions.

c) The term loan makes it possible to use commercial paper, and the agreement allows GMCLP to borrow up to $300,000,000; no repayments are required before the maturity date of April 30, 2005.

d) The Northern New England Gas Corporation ("NNEG") term note that was secured by the shares of its wholly-owned subsidiary, VGS was reimbursed on October 31, 2001.

e) This non-recourse term loan for the project's partners is secured by a direct charge on PNGTS' principal assets, including long-term customer contracts, and PNGTS' units held by its partners.

Interest rate swap agreements, for which the Partnership's share represents a nominal value of $62,304,000 (US$39,254,000), fixing the effective rate at 6.35%, have been concluded until March 2003. In anticipation of renewing its debt, PNGTS concluded new interest rate swap agreements starting in December 2002, maturing in December 2012, and fixing the effective interest rate at 5.72%. The Partnership's share of these agreements amounts to $49,187,000 (US$30,990,000).

f) TQM's first mortgage bonds are all secured by a fixed, specific first hypothec on the gas pipeline system and on service, transportation and gas sales contracts, and by a hypothec on the business and all other property and assets. Upon reimbursement by TQM of the Series G bonds maturing on September 22, 2005, and all series issued after September 30, 2002, if any, the Series H and I bonds will no longer be secured by these hypothecs.

g) On April 1, 2000, TQM's term loan, originally obtained for its system extension, was converted for an additional period of three years and is secured by hypothecs, as described in note f). The Partnership's interest in the maximum amount of this loan is $40,350,000 as at September 30, 2002, and $42,350,000 as at September 30, 2001.

h) GMCLP's subsidiaries can borrow up to $27,600,000 under term loan agreements, secured by a hypothec on the universality of their movable property and an immovable hypothec of $7,000,000 on an immovable property. For the most part, the term loans are bankers' acceptances. Certain subsidiaries have signed interest rate swaps covering the period from October 1, 2002 to September 30, 2003.

i) The preferred units, which are held by Gaz Métropolitain Plus, inc., a wholly owned subsidiary of Gaz Métropolitain, inc., are retractable and redeemable and have a non-cumulative return of 6.0%.

j) As at September 30, 2002 and 2001, unregulated activities, both related and unrelated to the energy sector, owned by GMCLP represented 2.0% and 1.9% respectively, of its total non-consolidated assets. GMCLP has undertaken not to increase its interest in such activities above 10.0% of its total non-consolidated assets pursuant to its trust deeds.

k) As at September 30, 2002 and 2001, interest coverage on consolidated long-term debt is respectively 2.85 times and 2.51 times and consolidated tangible net asset coverage on consolidated long-term debt, including current maturities, is respectively 1.64 times and 1.61 times.

## 10. PARTNERS' EQUITY

### AUTHORIZED

Unlimited number of units; each unit is equal in rank with any other unit and is entitled to the same rights, privileges and obligations.

| | **2002** | 2001 |
|---|---|---|
| **ISSUED AND FULLY PAID** | | |
| Number of units as at September 30, (in thousands of units) | **110,469** | 110,469 |

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 10. PARTNERS' EQUITY (CONT'D)

The agreements relating to the various long-term debt trust deeds provide that GMCLP will not make a distribution to its Partners if long-term debt exceeds 75% of total capitalization. The agreements also provide that GMCLP will not issue any new long-term debt if such debt would exceed 65% of total capitalization. GMCLP is in compliance with these covenants as at September 30, 2002 and 2001.

### UNIT OPTION PLAN

The Partnership has reserved 1,000,000 units for a unit option plan. Options can not be exercised before the first anniversary of a grant unless the Board of Directors determines otherwise when an option is granted. Options can be exercised at a cumulative rate of 25% on each of four anniversaries of the grant. Options expire seven years after the grant date. On November 15, 2000, GMCLP granted named executives 132,440 unit options at a price of $15.04. Because the condition stipulating that an average unit price of at least $17.35 had to be maintained for three consecutive months had been fulfilled, 33,110 units can be exercised as at September 30, 2002.

## 11. CASH FLOWS

a) Change in non-cash working capital items:

| | **2002** | 2001 |
|---|---|---|
| Trade and other receivables | **$ (735)** | $39,830 |
| Inventories | **1,512** | (9,305) |
| Prepaid expenses | **(9)** | 2,062 |
| Accounts payable and accrued liabilities | **24,562** | (7,028) |
| | **$25,330** | $25,559 |

b) Other information:

| | **2002** | 2001 |
|---|---|---|
| Interest received | **$ 3,027** | $ 2,078 |
| Interest paid | **$86,904** | $91,979 |

## 12. RESULTS

a) Overearnings from the activities of GMCLP-QDA amount to $27,061,000 for the fiscal year ended September 30, 2002. In accordance with the sharing method established by Decision D2000-183 dealing with the performance incentive mechanisms, the distributor (GMCLP-QDA) has included in income for the year its $9,020,000 share as incentive income that is subject to the final approval of the Régie following its review of the regulatory report that should be filed in December 2002. The balance of the overearnings presented as a liability in the balance sheet is shared by the customers and the Energy Efficiency Fund in the amounts of $12,731,000 and $5,310,000 respectively.

For the year ending September 30, 2001, there were no overearnings.

Following the review of the regulatory report for the year ended September 30, 2000, and based on the method for sharing overearnings, the Régie authorized the distributor to retain an amount of $3,024,000 as an incentive return, which is included in income of the 2001 year.

b) For the years ending September 30, 2002 and 2001, annual changes in the rate stabilization accounts represent net revenues of $50,491,000 and $5,274,000 respectively, which are included in the corresponding revenue, direct cost and interest on long-term debt accounts.

c) For the years ended September 30, 2002 and 2001, the operations and maintenance account includes current and future income taxes totaling $1,696,000 and $2,882,000 respectively for the subsidiaries and joint ventures.

Net income taxes payable and net future income taxes of $12,163,000 as at September 30, 2002, and $9,119,000 as at September 30, 2001, are presented in the balance sheet.

## 13. EMPLOYEE FUTURE BENEFITS

The Partnership maintains defined benefit or defined contribution pension plans that cover virtually all of its employees. The defined benefit plans are funded, which ensures that employees will receive a pension determined according to length of service and salaries during their highest earning years.

The Partnership also provides post-employment benefits other than pensions, including supplementary health and dental care and life insurance, for virtually all of its employees, their spouses and qualified dependants. These benefits are not funded.

The following tables describe the Partnership's employee future benefits-related obligations and expenses in accordance with the standards set out in Section 3461 of the CICA Handbook as well as the impact of the unrecorded transitional obligations of GMCLP-QDA:

| | **2002** | 2001 | **2002** | 2001 |
|---|---|---|---|---|
| | **Pension plans** | Pension plans | **Other post-employment benefits** | Other post-employment benefits |
| **ACCRUED BENEFIT OBLIGATION** | | | | |
| BALANCE, BEGINNING OF YEAR | **$256,324** | $209,278 | **$28,070** | $27,102 |
| Adjustment due to adoption of new standard (Note 2) | **–** | 350 | **–** | – |
| ADJUSTED BEGINNING BALANCE | **256,324** | 209,628 | **28,070** | 27,102 |
| Current service cost | **8,691** | 8,250 | **994** | 707 |
| Interest cost | **16,801** | 15,173 | **1,834** | 1,801 |
| Employee contributions | **2,681** | 2,455 | **–** | – |
| Benefits paid and reimbursements | **(17,780)** | (12,093) | **(1,918)** | (1,804) |
| Plan amendment costs | **1,162** | 24,648 | **–** | – |
| Actuarial loss (gain) | **91** | 7,871 | **(341)** | 264 |
| Foreign exchange variations | **49** | 392 | **–** | – |
| BALANCE, END OF YEAR | **268,019** | 256,324 | **28,639** | 28,070 |
| **PLAN ASSETS AT FAIR VALUE** | | | | |
| BALANCE, BEGINNING OF YEAR | **268,089** | 245,328 | **–** | – |
| Adjustment due to adoption of new standard [1] (Note 2) | **–** | 42,011 | **–** | – |
| ADJUSTED BALANCE, BEGINNING OF YEAR | **268,089** | 287,339 | **–** | – |
| Actual return on plan assets | **1,193** | (12,190) | **–** | – |
| Employer contributions | **3,252** | 2,236 | **–** | – |
| Employee contributions | **2,681** | 2,455 | **–** | – |
| Benefits paid and reimbursements | **(17,780)** | (12,093) | **–** | – |
| Foreign exchange variations | **30** | 342 | **–** | – |
| BALANCE, END OF YEAR | **257,465** | 268,089 | **–** | – |
| **EXCESS (DEFICIENCY) OF ASSETS VERSUS OBLIGATIONS** | **(10,554)** | 11,765 | **(28,639)** | (28,070) |
| Unamortized past service costs | **23,331** | 24,173 | **–** | – |
| Unamortized net actuarial loss (gain) | **59,054** | 41,547 | **(60)** | 264 |
| Unamortized transitional obligation (asset) | **(69,670)** | (75,453) | **20,361** | 22,213 |
| **ACCRUED BENEFIT ASSET (OBLIGATION), BASED ON CICA** | **$ 2,161** | $ 2,032 | **$ (8,338)** | $ (5,593) |
| Representing: | | | | |
| Accrued benefit asset (obligation) of GMCLP-QDA unrecognized | **$ 6,716** | $ 4,954 | **$ (6,715)** | $ (2,915) |
| Accrued benefit obligation recognized | **(4,555)** | (2,922) | **(1,623)** | (2,678) |
| | **$ 2,161** | $ 2,032 | **$ (8,338)** | $ (5,593) |

(1) Pension plan assets are valued at their fair value at the balance sheet date. Previously they were valued at an average market value and fluctuations were allocated over a five-year period.

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 13. EMPLOYEE FUTURE BENEFITS (CONT'D)

### MAIN ACTUARIAL ASSUMPTIONS

| | 2002 Pension plans | 2001 Pension plans | 2002 Other post-employment benefits | 2001 Other post-employment benefits |
|---|---|---|---|---|
| Discount rate | **6.50%** | 6.50% | **6.50%** | 6.50% |
| Expected long-term rate of return on plan assets | **7.50%** | 7.75% | **–** | – |
| Rate of compensation increase | **3.50%** | 3.50% | **3.50%** | 3.50% |

### THE PARTNERSHIP'S NET EMPLOYEE FUTURE BENEFIT EXPENSE IS AS FOLLOWS:

| | 2002 Pension plans | 2001 Pension plans | 2002 Other post-employment benefits | 2001 Other post-employment benefits |
|---|---|---|---|---|
| Current service cost | **$ 8,691** | $ 8,250 | **$ 994** | $ 707 |
| Interest cost | **16,801** | 15,173 | **1,834** | 1,801 |
| Expected return on plan assets | **(19,651)** | (21,926) | **–** | – |
| Amortization of past service costs | **2,004** | 828 | **–** | – |
| Amortization of net actuarial losses (gains) | **1,061** | – | **(17)** | – |
| Amortization of transitional obligation (asset) | **(5,783)** | (5,501) | **1,852** | 1,852 |
| Net employee future benefit expense (income), based on CICA | **$ 3,123** | $ (3,176) | **$4,663** | $4,360 |
| Representing: | | | | |
| Expense (revenue) of GMCLP-QDA | **$ (897)** | $ (4,598) | **$3,705** | $3,509 |
| Net expense recognized | **4,020** | 1,422 | **958** | 851 |
| | **$ 3,123** | $ (3,176) | **$4,663** | $4,360 |

GMCLP-QDA's employee future benefits expense on a cash basis for pension plans is $2,663,000 in 2002 and $988,000 in 2001 and for other post-employment benefits is $822,000 in 2002 and $792,000 in 2001.

The expense for defined contribution and other plans is $395,000 in 2002 and $747,000 in 2001.

## 14. REGULATORY AND TAX POSITION

For regulatory purposes for GMCLP-QDA, only current income taxes payable are deemed and taken into account in setting rates. For income tax purposes, GMCLP has claimed capital cost allowance and certain other deductions relating to deferred charges that have the effect of reducing the Partners' income for tax purposes, thereby deferring to future years income taxes otherwise payable by the Partners.

The amount of these future income taxes, and the taxes related to GMCLP's ownership interest in TQM relating to the regulated activities and not recognized by the Partnership, are calculated in accordance with the balance sheet method in Section 3465 of the CICA Handbook. Under this method, future income taxes are determined based on the differences between the accounting and tax bases of assets and liabilities. The future income tax assets and liabilities are calculated at the tax rate for a taxable Canadian corporation that should be in effect during the year in which the temporary differences should be realized or settled.

The net future income tax liability amounts to $124,435,000 as at September 30, 2002, and to $132,676,000 as at September 30, 2001. The reversal of the future income taxes for the year and the future income taxes receivable arising as a result of non-deductible provisions for the year, amounts to $8,241,000. The Régie and the NEB should allow these future income taxes to be included in rates when the temporary differences reverse, with the exception of amounts of $2,824,000 as at September 30, 2002, and $6,126,000 as at September 30, 2001, arising primarily from the 1991 reorganization.

## 15. SEGMENTED DATA

The business sectors presented are segmented in line with the way management organizes the various segments within the Partnership for the purposes of operational decision-making and performance assessment.

GMCLP has the three following reportable segments:

**DISTRIBUTION:** Delivers natural gas to users;
**TRANSPORTATION:** Transports natural gas, generally from the producers to the distributor;
**ENERGY SERVICE AND OTHER:** Includes unregulated activities of energy and technology services, sale, leasing, financing and maintenance of gas appliances, and water and waste water system diagnoses and repairs.

The accounting policies for these segments are the same as those described in Note 1. The Partnership assesses performance based on operating income before income taxes.

The Partnership records inter-segment sales and transfers as though they were made to a third party, i.e. at market value.

| | | | | | 2002 |
|---|---|---|---|---|---|
| | Distribution | Transportation | Energy services and other | Non-allocated expenses and eliminations | Total |
| Customer revenues | $1,487,134 | $ 62,135 | $48,752 | $ – | $1,598,021 |
| Inter-segment revenues | 1,719 | 696 | 5,577 | (7,992) | – |
| Interest income (a) | 8,156 | – | 1,623 | (100) | 9,679 |
| Total revenues | 1,497,009 | 62,831 | 55,952 | (8,092) | 1,607,700 |
| Direct costs | 1,020,437 | – | 37,926 | (6,535) | 1,051,828 |
| Gross margin | 476,572 | 62,831 | 18,026 | (1,557) | 555,872 |
| Operations and maintenance expenses | 150,977 | 13,936 | 12,496 | (740) | 176,669 |
| Earnings before interest, taxes, depreciation and amortization (EBITDA) | 325,595 | 48,895 | 5,530 | (817) | 379,203 |
| Depreciation and amortization | 113,655 | 17,807 | 3,716 | 33 | 135,211 |
| Interest expense | 69,870 | 18,246 | 1,871 | (575) | 89,412 |
| Partners' income | $ 142,070 | $ 12,842 | $ (57) | $ (275) | $ 154,580 |
| Assets | $1,856,445 | $422,686 | $80,817 | $(10,060) | $2,349,888 |
| Additions to | | | | | |
| Property, plant and equipment | $ 88,455 | $ 2,332 | $ 4,168 | $ – | $ 94,955 |
| Deferred charges | 28,152 | (3,442) | 8 | – | 24,718 |
| | $ 116,607 | $ (1,110) | $ 4,176 | $ – | $ 119,673 |
| Goodwill | | | | | |
| Balance, beginning | 9,370 | $ 7,596 | $ 7,036 | $ – | $ 24,002 |
| Impairment loss (Note 2) | – | – | (2,919) | – | (2,919) |
| Adjusted balance, beginning | 9,370 | 7,596 | 4,117 | – | 21,083 |
| Translation adjustment | 59 | – | – | – | 59 |
| Acquisitions | – | – | 1,921 | – | 1,921 |
| Balance, end | $ 9,429 | $ 7,596 | $ 6,038 | $ – | $ 23,063 |

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 15. SEGMENTED DATA (CONT'D)

2001

| | Distribution | Transportation | Energy services and other | Non-allocated expenses and eliminations | Total |
|---|---|---|---|---|---|
| Customer revenues | $1,962,585 | $ 60,002 | $42,306 | $ – | $2,064,893 |
| Inter-segment revenues | 677 | 668 | 4,906 | (6,251) | – |
| Interest income (a) | 3,958 | 297 | 829 | – | 5,084 |
| Total revenues | 1,967,220 | 60,967 | 48,041 | (6,251) | 2,069,977 |
| Direct costs | 1,506,051 | – | 32,764 | (5,899) | 1,532,916 |
| Gross margin | 461,169 | 60,967 | 15,277 | (352) | 537,061 |
| Operations and maintenance expenses | 143,071 | 11,354 | 11,273 | 1,802 | 167,500 |
| EBITDA | 318,098 | 49,613 | 4,004 | (2,154) | 369,561 |
| Depreciation and amortization | 107,789 | 16,420 | 2,704 | 198 | 127,111 |
| Interest expense | 75,755 | 22,890 | 2,659 | (18) | 101,286 |
| Partners' income | $ 134,554 | $ 10,303 | $ (1,359) | $ (2,334) | $ 141,164 |
| Assets | $1,852,942 | $440,658 | $67,579 | $(11,483) | $2,349,696 |
| Additions to | | | | | |
| Property, plant and equipment | $ 73,860 | $ 2,585 | $ 4,388 | $ – | $ 80,833 |
| Deferred charges | 168,547 | 1,660 | 385 | 1,478 | 172,070 |
| | $ 242,407 | $ 4,245 | $ 4,773 | $ 1,478 | $ 252,903 |
| Goodwill | | | | | |
| Balance, beginning | $ 10,084 | $ 8,031 | $ 6,583 | $ – | $ 24,698 |
| Translation adjustment | 460 | – | – | – | 460 |
| Acquisitions | – | – | 820 | – | 820 |
| | 10,544 | 8,031 | 7,403 | – | 25,978 |
| Disposal | (804) | – | – | – | (804) |
| Amortization | (370) | (435) | (367) | – | (1,172) |
| Balance, end | $ 9,370 | $ 7,596 | $ 7,036 | $ – | $ 24,002 |

Only the distribution sector includes significant items other than depreciation and amortization that have no impact on cash flows, i.e. rate stabilization accounts and reduction in deferred charges related to cost of natural gas as specifically shown in the cash flow statement.

a) Distribution interest income arises mainly from the capitalized return on assets not included in the rate base in accordance with regulatory provisions.

### GEOGRAPHIC INFORMATION

| | **2002** | | 2001 | |
|---|---|---|---|---|
| | **Revenues** | **Fixed assets and goodwill** | Revenues | Fixed assets and goodwill |
| Canada | **$1,492,231** | **$1,543,721** | $1,956,385 | $1,547,735 |
| United States | **115,469** | **238,020** | 113,592 | 226,967 |
| Total | **$1,607,700** | **$1,781,741** | $2,069,977 | $1,774,702 |

## 16. RELATED PARTY TRANSACTIONS

During the year, GMCLP concluded the following transactions with related parties in the normal course of business, as authorized by the Régie. The amounts received from or paid to related parties are determined based on contracts between the parties and in which the value of the services rendered has been established at the exchange amount:

| | 2002 | 2001 |
|---|---|---|
| Purchase of natural gas from one of the ultimate shareholders of Gaz Métropolitain, inc. | **$13,227** | $21,384 |
| Storage service owned in part by one of the ultimate shareholders of Gaz Métropolitain, inc. | **$14,079** | $15,973 |

As at September 30, 2002 and 2001, transactions with the parent company, Gaz Métropolitain, inc. (hereinafter "GMi"), and companies owned by its ultimate shareholder represent a net amount payable of $2,601,000 and $4,181,000 included in accounts payable and accrued liabilities, and trade and other receivables. Under the partnership agreement, GMCLP pays management fees of $50,000 annually to GMi.

As of October 1, 2000, GMCLP transferred 100% of the shares of its subsidiary, CCUM, to Gaz Métropolitain Plus inc. (hereinafter "GMPi"), a wholly-owned subsidiary of GMi, in exchange for $7,396,000 preferred shares of GMPi. In addition, GMPi's assets were transferred to Climatisation et Chauffage Urbains de Montréal, s.e.c. (hereinafter "CCUM, s.e.c.") in exchange for preferred units of CCUM, s.e.c. having a value of $7,366,000. These transactions were recorded at the carrying amount.

## 17. FINANCIAL INSTRUMENTS

The fair value of the financial instruments represents the estimated amounts that the Partnership would receive or pay to cancel these financial instruments as at the date of the financial statements. The Partnership does not hold or issue derivative financial instruments for speculative purposes.

### FINANCIAL INSTRUMENTS INCLUDED IN BALANCE SHEET

Cash, trade and other receivables, bank borrowings as well as accounts payable and accrued liabilities are short-term financial instruments whose fair value approximates the carrying amount given that they will mature shortly.

#### FAIR VALUE OF LONG-TERM DEBT

The fair value of the long-term debt, including current instalments, is calculated using stock exchange prices at the end of the year or discounted cash flows using interest rates which GMCLP, its subsidiaries and its joint ventures could have obtained as at the balance sheet date for loans with similar terms, conditions and maturity dates.

| | 2002 | | 2001 | |
|---|---|---|---|---|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| **LONG-TERM DEBT** | | | | |
| GMCLP | **$ 928,628** | **$1,049,580** | $ 940,345 | $1,028,434 |
| NNEG | **99,851** | **104,391** | 115,405 | 122,017 |
| TQM | **182,850** | **192,022** | 184,850 | 190,555 |
| Other | **29,782** | **29,782** | 29,724 | 29,724 |
| | **$1,241,111** | **$1,375,775** | $1,270,324 | $1,370,730 |

(ALL TABULAR AMOUNTS ARE IN THOUSANDS OF DOLLARS.)

## 17. FINANCIAL INSTRUMENTS (CONT'D)

### OFF-BALANCE SHEET FINANCIAL INSTRUMENTS

The Partnership uses various types of derivative financial instruments to stabilize the cost of gas and swap agreements to hedge against interest rate fluctuations. The Partnership obtains an independent valuation of the market value of these financial instruments. The valuation is based on published indices at the closing date, volatility and expiration dates.

Derivatives used by GMCLP-QDA to stabilize the cost of system gas comply with the parameters approved by the Régie. Gains or losses attributable to financial instruments used by GMCLP-QDA are reimbursed or recovered through gas supply rates in accordance with the method approved by the Régie.

Gains or losses attributable to other financial instruments are deferred and recognized in income under revenues and expenses arising from the corresponding hedged positions on the basis allowed by the Régie.

The Partnership only concludes off-balance sheet hedge transactions with major financial institutions that meet its credit evaluation standards.

Management considers that these derivative financial instruments do not present any unusual risk and does not expect any significant gain or loss as a result of these transactions.

FAIR VALUE OF OFF-BALANCE SHEET FINANCIAL INSTRUMENTS THAT ARE SENSITIVE TO INTEREST RATE:

| | **2002** | 2001 |
|---|---|---|
| | **Fair value (payable)** | Fair value (payable) |
| **INTEREST RATE** | | |
| Swaps related to long-term debt (Note 9e) | | |
| Contracts maturing in April 2003 | **$(1,580)** | $(2,542) |
| Contracts maturing in December 2012 | **(5,524)** | – |
| | **$(7,104)** | $(2,542) |

FAIR VALUE OF OFF-BALANCE SHEET FINANCIAL INSTRUMENTS THAT ARE SENSITIVE TO GAS PRICES:
The estimated market value of derivative instruments related to the price of gas fluctuates daily based on the volatility of natural gas prices and the period covered by the instruments.

| | | | | **2002** | 2001 |
|---|---|---|---|---|---|
| | | | | **Fair value receivable (payable)** | Fair value (payable) |
| | | | | **Maturity** | |
| | **2003** | **2004** | **2005** | **Total** | 2002 to 2004 |
| **GAS PRICES** | | | | | |
| Contracts: | | | | | |
| Swaps | **$(8,300)** | **$(4,103)** | **$(302)** | **$(12,705)** | $(41,980) |
| Calls | **(6,924)** | **(3,724)** | **(290)** | **(10,938)** | (43,442) |
| Collars | **1,606** | **115** | **–** | **1,721** | (6,947) |
| Three-way collars | **4,829** | **1,094** | **58** | **5,981** | – |
| | **$(8,789)** | **$(6,618)** | **$(534)** | **$(15,941)** | $(92,369) |

| | 2003 | 2004 | 2005 | 2002<br>Thousands of gigajoules<br>Maturity<br>Total | 2001<br>Thousands of gigajoules<br><br>2002 to 2004 |
|---|---|---|---|---|---|
| **VOLUMES COVERED** | | | | | |
| Swaps | **10,728** | **5,409** | **349** | **16,486** | 18,994 |
| Calls | **7,300** | **3,970** | **310** | **11,580** | 20,545 |
| Collars | **3,880** | **248** | **–** | **4,128** | 3,573 |
| Three-way collars | **25,924** | **11,826** | **1,019** | **38,769** | – |
| | **47,832** | **21,453** | **1,678** | **70,963** | 43,112 |

As at September 30, 2002, the Partnership is not planning to cancel any financial instruments before the maturity date.

## 18. COMMITMENTS AND CONTINGENCIES

a) In the normal course of business, the Partnership signed supply, transportation and storage contracts for periods up to 2013. The costs relating to these contracts will be included in rates in the corresponding periods.

b) GMCLP is cited in claims and lawsuits in the normal course of its activities. In the opinion of management, these claims and lawsuits are, for the most part, covered by appropriate insurance coverage and the overall amount of the contingent liability relating to these claims and lawsuits is not material.

c) The NNEG subsidiary has been cited in a lawsuit, jointly with others, following the discovery of polluting substances on land it once owned for a brief period of time during the 1960s. The investigation by the U.S. Environmental Protection Agency has not been completed and NNEG is unable to predict the outcome of the lawsuit at this time. In the event a claim arises, an application will be filed with the Vermont Public Service Board to seek recovery through the rates of VGS. Moreover, an agreement was reached, in 1994, between NNEG and a third party limiting the maximum amount payable by NNEG. In the opinion of management, any costs resulting from this claim would not be significant for the Partnership.

d) Upon completion of the construction of the TQM pipeline extension to the U.S. border, the project manager of the construction work lodged a claim against TQM for reimbursement of the contractor's cost overruns. This claim is presently under arbitration to determine the merits and the quantum of the claim. The contractor also registered a legal hypothec on TQM's pipeline, the result of which depends on the merits of the claim and the non-payment of the debt by TQM, which is unlikely. GMCLP does not expect the arbitrator's decision will have a significant financial impact on the pipeline's profitability or on the Partnership's overall financial situation.

## 19. SUBSEQUENT EVENTS

Distributions totalling $35,350,000 or $0.32 per unit, were paid to Partners on October 1, 2002.

## 20. COMPARATIVE DATA

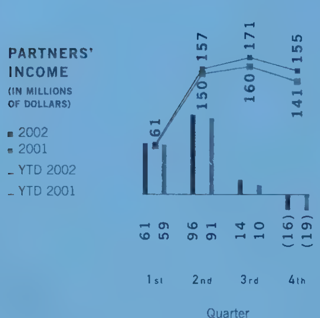
Certain comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year.

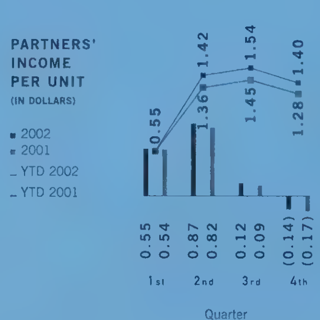
# QUARTERLY CONSOLIDATED FINANCIAL INFORMATION [1][2]

| Years ended September 30, (in thousands of dollars) | 1st | 2nd | 3rd | 4th | 2002 Year |
|---|---|---|---|---|---|
| Revenues | $484,318 | $601,417 | $310,523 | $211,442 | $1,607,700 |
| Gross margin | $161,283 | $198,904 | $116,345 | $ 79,340 | $ 555,872 |
| Partners' income | $ 60,697 | $ 96,369 | $ 13,538 | $ (16,024) | $ 154,580 |
| Diluted and basic Partners' income per unit (in dollars) | $ 0.55 | $ 0.87 | $ 0.12 | $ (0.14) | $ 1.40 |
| Distributions paid (in dollars) | $ 0.32 | $ 0.32 | $ 0.32 | $ 0.32 | $ 1.28 |
| Partners' equity per unit (in dollars) | $ 7.59 | $ 8.14 | $ 7.89 | $ 7.45 | $ 7.45 |
| Market prices on Toronto Stock exchange (in dollars): | | | | | |
| High | $ 18.00 | $ 17.99 | $ 17.98 | $ 18.32 | $ 18.32 |
| Low | $ 16.50 | $ 17.05 | $ 16.28 | $ 17.50 | $ 16.28 |
| Close | $ 17.60 | $ 17.23 | $ 17.71 | $ 18.10 | $ 18.10 |
| Number of units oustanding (in millions) | 110.5 | 110.5 | 110.5 | 110.5 | 110.5 |

| | 1st | 2nd | 3rd | 4th | 2001 Year |
|---|---|---|---|---|---|
| Revenues | $ 654,799 | $ 799,945 | $ 374,715 | $ 240,518 | $ 2,069,977 |
| Gross margin | $ 162,901 | $ 191,946 | $ 108,306 | $ 73,908 | $ 537,061 |
| Partners' income | $ 59,322 | $ 90,574 | $ 9,841 | $ (18,573) | $ 141,164 |
| Diluted and basic Partners' income per unit (in dollars) | $ 0.54 | $ 0.82 | $ 0.09 | $ (0.17) | $ 1.28 |
| Distributions paid (in dollars) | $ 0.31 | $ 0.32 | $ 0.32 | $ 0.32 | $ 1.27 |
| Partners' equity per unit (in dollars) | $ 7.52 | $ 8.07 | $ 7.80 | $ 7.35 | $ 7.35 |
| Market prices on Toronto Stock exchange (in dollars): | | | | | |
| High | $ 15.95 | $ 16.74 | $ 16.50 | $ 16.90 | $ 16.90 |
| Low | $ 14.80 | $ 15.85 | $ 15.85 | $ 15.85 | $ 14.80 |
| Close | $ 15.80 | $ 16.00 | $ 16.05 | $ 16.35 | $ 16.35 |
| Number of units oustanding (in millions) | 110.5 | 110.5 | 110.5 | 110.5 | 110.5 |

(1) Unaudited quarterly data.
(2) Seasonal temperature fluctuations affect GMCLP's quarterly financial results, as the following charts show.



| Years ended September 30, | **2002** | 2001 | 2000 | 1999 | 1998 |
|---|---|---|---|---|---|
| **NORMALIZED VOLUME** ($10^6m^3$) [2] | | | | | |
| DISTRIBUTION | | | | | |
| Industrial | | | | | |
| Firm service | **2,139** | 2,182 | 2,377 | 2,372 | 2,549 |
| Interruptible service | **1,124** | 841 | 1,414 | 1,354 | 1,369 |
| Commercial | **1,971** | 1,910 | 1,986 | 1,883 | 1,717 |
| Residential | **739** | 743 | 782 | 759 | 726 |
| Total ($10^6m^3$) | **5,973** | 5,676 | 6,559 | 6,368 | 6,361 |
| Total (Bcf) | **211** | 200 | 232 | 225 | 225 |
| **NATURAL GAS DELIVERIES** ($10^6m^3$) | | | | | |
| DISTRIBUTION | | | | | |
| Total ($10^6m^3$) | **5,680** | 5,639 | 6,348 | 6,123 | 6,169 |
| Total (Bcf) | **200** | 199 | 224 | 216 | 218 |
| TRANSPORTATION [3][4] | | | | | |
| Total ($10^6m^3$) | **6,439** | 6,023 | 5,855 | 3,928 | 3,335 |
| Total (Bcf) | **227** | 213 | 207 | 139 | 118 |
| **CUSTOMERS (DISTRIBUTION)** | | | | | |
| Industrial | **2,198** | 2,109 | 2,038 | 2,095 | 2,062 |
| Commercial | **46,630** | 45,860 | 45,307 | 43,826 | 42,285 |
| Residential | **137,972** | 136,520 | 136,117 | 133,734 | 133,587 |
| Total | **186,800** | 184,489 | 183,462 | 179,655 | 177,934 |
| **SYSTEM DATA** | | | | | |
| Length of pipelines (in km) | | | | | |
| DISTRIBUTION | | | | | |
| Canada | **9,166** | 8,999 | 8 ,775 | 8,493 | 8,328 |
| United States | **895** | 853 | 828 | 815 | 787 |
| Total | **10,061** | 9,852 | 9,603 | 9,308 | 9,115 |
| TRANSPORTATION [4] | | | | | |
| Canada | **670** | 670 | 670 | 670 | 453 |
| United States | **489** | 489 | 489 | 474 | – |
| Total | **1,159** | 1,159 | 1,159 | 1,144 | 453 |
| Gross property, plant and equipment (in millions of dollars) | **2,636** | 2,556 | 2,477 | 2,396 | 2,235 |
| Net property, plant and equipment (in millions of dollars) | **1,759** | 1,751 | 1,741 | 1,727 | 1,628 |
| Additions to property, plant, equipment and deferred charges (in millions of dollars) | **120** | 253 | 139 | 235 | 256 |
| **NUMBER OF EMPLOYEES** [4] | | | | | |
| DISTRIBUTION | | | | | |
| GMCLP | **1,194** | 1,182 | 1,300 | 1,292 | 1,276 |
| NNEG | **112** | 108 | 147 | 144 | 154 |
| | **1,306** | 1,290 | 1,447 | 1,436 | 1,430 |
| TRANSPORTATION | | | | | |
| TQM | **60** | 60 | 70 | 66 | 65 |
| PNGTS | **32** | 31 | 29 | 29 | 17 |
| | **92** | 91 | 99 | 95 | 82 |
| ENERGY SERVICES AND OTHER | | | | | |
| AQUA DATA | **63** | 61 | 57 | 59 | – |
| AQUA-REHAB | **32** | 33 | 29 | 40 | – |
| CCUM | **19** | 16 | 24 | 21 | 21 |
| CONSULGAZ | **6** | 3 | 4 | 3 | 2 |
| GAZ MÉTROPOLITAIN PLUS [5] | **102** | 92 | 89 | 26 | 24 |
| OPTION GAZ | **18** | 17 | 18 | – | – |
| SERVITECH COMBUSTION | **70** | – | – | – | – |
| SOFAME | **18** | 18 | 22 | 23 | – |
| SOGENER | **15** | 14 | 11 | 5 | 1 |
| TELDIG | **12** | 12 | 8 | 8 | – |
| | **355** | 266 | 262 | 185 | 48 |

(1) Unaudited data.
(2) Normalized volumes based on normal temperature for natural gas distribution in Québec.
(3) Includes volumes transported and delivered by TQM to the distribution sector (GMCLP) and PNGTS.
(4) Data not adjusted for GMCLP's percentage interest in the subsidiaries and joint ventures.
(5) Previously GMPLP before 2000.

| Years ended September 30, (in thousands of dollars) | 2002 | 2001 | 2000 |
|---|---|---|---|
| **SUMMARY OF RESULTS** | | | |
| Revenues | **$1,607,700** | $2,069,977 | $1,633,736 |
| Direct costs | **1,051,828** | 1,532,916 | 1,100,310 |
| Gross margin | **555,872** | 537,061 | 533,426 |
| Operations and maintenance[1] | **176,669** | 167,500 | 176,109 |
| Operating income before depreciation and amortization | **379,203** | 369,561 | 357,317 |
| Depreciation and amortization | **135,211** | 127,111 | 120,797 |
| Operating income | **243,992** | 242,450 | 236,520 |
| Financial expense | **89,412** | 101,286 | 92,798 |
| PARTNERS' INCOME | **$ 154,580** | $ 141,164 | $ 143,722 |
| **CASH FLOWS** | | | |
| Operating activities (including working capital) | **$ 311,567** | $ 323,018 | $ 190,003 |
| Investing activities | **(124,063)** | (257,893) | (142,657) |
| Financing activities: | | | |
| Distributions paid to Partners | **(141,400)** | (140,295) | (136,981) |
| Other financing activities | **(39,172)** | 74,797 | 84,513 |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | **$ 6,932** | $ (373) | $ (5,122) |
| **PER UNIT DATA**[2] | | | |
| Partners' income (in dollars) | **$ 1.40** | $ 1.28 | $ 1.30 |
| Operating cash flows based on weighted average number of units outstanding (in dollars) | **$ 2.82** | $ 2.92 | $ 1.72 |
| Distribution paid (in dollars) | **$ 1.28** | $ 1.27 | $ 1.24 |
| Partners' equity (in dollars) | **$ 7.45** | $ 7.35 | $ 7.30 |
| Weighted average number of units outstanding (in thousands) | **110,469** | 110,469 | 110,469 |
| Number of units outstanding as at September 30 (in thousands) | **110,469** | 110,469 | 110,469 |
| **FINANCIAL STRUCTURE** | | | |
| Debt maturing within one year | **$ 44,351** | $ 3,099 | $ 3,722 |
| Long-term debt | **1,196,760** | 1,267,225 | 1,189,766 |
| Total debt | **1,241,111** | 1,270,324 | 1,193,488 |
| Partners' equity | **822,655** | 811,845 | 805,960 |
| TOTAL | **$2,063,766** | $2,082,169 | $1,999,448 |
| **TOTAL DEBT / TOTAL CAPITALIZATION** | **60.1%** | 61.0% | 59.7% |
| **INTEREST COVERAGE RATIO ON CONSOLIDATED LONG-TERM DEBT** | **2.8** | 2.5 | 2.7 |
| **TOTAL ASSETS** | **$2,349,888** | $2,349,696 | $2,262,939 |
| **FINANCIAL INFORMATION RELATED TO DETERMINATION OF RATE OF RETURN OF GMCLP–QDA BY THE RÉGIE DE L'ÉNERGIE**[4][5] | | | |
| Rate base[6] | **$1,545,596** | $1,545,839 | $1,486,889 |
| Deemed common equity[6] | **38.50%** | 38.50% | 38.50% |
| Authorized rate of return on deemed common equity | **9.69%** | 10.38% | 9.72% |
| Deemed preferred equity[6] | **7.50%** | 7.17% | 7.45% |
| Authorized rate of return on deemed preferred equity | **4.54%** | 5.37% | 5.61% |
| Deemed tax expense | **$ 61,787** | $ 60,350 | $ 63,890 |

(1) Includes development activities.
(2) GMCLP has been a listed partnership since 1993.
(3) Pro forma net income of $1.15 calculated as if the net income for the initial Partners until January 31, 1993 had been distributed on the first day of the fiscal year and as if the units had been issued on the same date.

| 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 |
|---|---|---|---|---|---|---|
| $1,339,022 | $1,216,923 | $1,197,742 | $1,117,600 | $1,088,164 | $1,221,470 | $1,050,361 |
| 841,367 | 736,063 | 722,052 | 643,278 | 628,196 | 788,566 | 654,882 |
| 497,655 | 480,860 | 475,690 | 474,322 | 459,968 | 432,904 | 395,479 |
| 164,556 | 159,246 | 158,369 | 145,171 | 149,464 | 144,492 | 143,190 |
| 333,099 | 321,614 | 317,321 | 329,151 | 310,504 | 288,412 | 252,289 |
| 106,834 | 100,788 | 92,358 | 87,634 | 82,006 | 78,366 | 67,886 |
| 226,265 | 220,826 | 224,963 | 241,517 | 228,498 | 210,046 | 184,403 |
| 90,493 | 80,080 | 86,256 | 95,689 | 93,490 | 86,433 | 73,035 |
| $ 135,772 | $ 140,746 | $ 138,707 | $ 145,828 | $ 135,008 | $ 123,613 | $ 111,368 |
| $ 246,539 | $ 231,691 | $ 246,294 | $ 298,436 | $ 253,324 | $ 225,667 | $ 222,567 |
| (242,372) | (265,771) | (118,823) | (145,530) | (241,226) | (244,029) | (193,129) |
| (134,748) | (138,459) | (142,200) | (141,666) | (132,893) | (120,931) | (172,444) |
| 111,620 | 198,432 | 17,000 | (18,240) | 120,489 | 136,929 | 152,676 |
| $ (18,961) | $ 25,893 | $ 2,271 | $ (7,000) | $ (306) | $ (2,364) | $ 9,670 |
| $ 1.25 | $ 1.32 | $ 1.30 | $ 1.36 | $ 1.30 | $ 1.24 | $ 1.15[3] |
| $ 2.27 | $ 2.17 | $ 2.30 | $ 2.79 | $ 2.43 | $ 2.27 | $ 2.40 |
| $ 1.25 | $ 1.30 | $ 1.33 | $ 1.33 | $ 1.34 | $ 1.17 | $ 0.48 |
| $ 7.21 | $ 6.93 | $ 6.85 | $ 6.87 | $ 6.83 | $ 6.50 | $ 6.21 |
| 108,671 | 106,918 | 106,918 | 106,918 | 104,215 | 99,350 | 92,704 |
| 110,469 | 106,918 | 106,918 | 106,918 | 106,918 | 100,708 | 96,508 |
| $ 11,321 | $ 10,053 | $ 26,023 | $ 12,071 | $ 81,300 | $ 56,220 | $ 4,023 |
| 1,082,376 | 1,034,770 | 819,829 | 841,934 | 767,467 | 738,961 | 615,132 |
| 1,093,697 | 1,044,823 | 845,852 | 854,005 | 848,767 | 795,181 | 619,155 |
| 796,823 | 740,943 | 732,148 | 734,903 | 730,329 | 654,415 | 598,861 |
| $1,890,520 | $1,785,766 | $1,578,000 | $1,588,908 | $1,579,096 | $1,449,596 | $1,218,016 |
| 57.9% | 58.5% | 53.6% | 53.7% | 53.8% | 54.9% | 50.8% |
| 2.6 | 2.9 | 2.7 | 2.7 | 2.5 | 2.5 | 2.6 |
| $2,137,998 | $2,017,255 | $1,775,254 | $1,749,361 | $1,760,611 | $1,647,436 | $1,376,981 |
| $1,413,245 | $1,397,303 | $1,352,240 | $1,340,108 | $1,318,244 | $1,228,911 | $1,177,978 |
| 38.50% | 38.53% | 39.39% | 38.14% | 37.99% | 38.26% | 39.13% |
| 9.64% | 10.75% | 11.50% | 12.00% | 12.00% | 12.00% | 12.50% |
| 7.50% | 7.50% | 7.64% | 7.60% | 7.40% | 7.33% | 7.50% |
| 5.88% | 5.63% | 5.36% | 6.43% | 6.74% | 5.80% | 5.73% |
| $ 55,716 | $ 56,817 | $ 56,954 | $ 59,100 | $ 45,322 | $ 47,776 | $ 44,825 |

(4) Unaudited data.

(5) As noted under the accounting policies in the consolidated financial statements of GMCLP–QDA under Regulation.

(6) Calculated on a monthly average based on capitalization that differs from the financial structure as recorded in the balance sheet of GMCLP due to the inclusion of short-term financing, securitization of trade receivables and other items.

Gaz Métropolitain, inc. (the "Company") is essentially devoted to managing the affairs of Gaz Métropolitain and Company, Limited Partnership (the "Partnership") as its General Partner. The terms "Company" and "Partnership" are used interchangeably hereinafter. As part of this responsibility, and in accordance with the requirements of the Toronto Stock Exchange on which the Partnership's units are traded, that the Board of Directors summarizes in the following text its corporate governance policies and practices in relation to the Stock Exchange guidelines (summarized below and shown in bold). This statement, which was revised on November 20, 2002, meets the guidelines.

The Company, which holds 77.4% of the units of the Partnership, is a wholly-owned subsidiary of Noverco Inc.

1. **The board of directors of every corporation should explicitly assume responsibility for the stewardship of the corporation.** The Board is responsible for supervising the management of the business with the objective of ensuring that its resources and potential are used and exploited in such a way as to create value for the Partners, in accordance with applicable laws, standards and social responsibility. This growth objective includes protecting the value of the business against the main risks with which it is faced.

   **More particularly, the board should assume responsibility for:**
   **a) adoption of a strategic planning process.** Every two years, a multi-year strategic plan is prepared by management and submitted to the Board for discussion and approval. The plan is monitored periodically by comparing results with the strategies adopted. If appropriate, the strategies are adjusted.

   **b) the identification of the principal risks of the corporation's business and ensuring the implementation of appropriate systems to manage these risks.** The Board ensures, particularly through its Audit Committee, that management identifies the risks to which the Partnership is exposed and takes the necessary steps to manage or transfer such risks if they cannot be eliminated.

   **c) succession planning, including appointing, training and monitoring senior management.** The Human Resources Committee has the prime responsibility for evaluating candidates for the position of President and Chief Executive Officer and candidates proposed by the President and Chief Executive Officer for the other senior executive positions. This responsibility includes monitoring the performance and development of the incumbents and ensuring their succession is planned.

   **d) a communication policy for the corporation.** The Board, in particular the Audit Committee, ensures that the financial information for the Partners and the investing public is complete and objective, and that it is disseminated within the timeframe established by the Canadian securities commissions and the Stock Exchange. To discharge this responsibility, the Audit Committee reviews the annual and quarterly reports and related press releases, the annual information form and prospectuses.

   Financial information is disclosed through the normal channels and can be found in the "Investors' Sheet" section on the Partnership's Internet site. Any Partner wishing to ask the Partnership for additional information or provide it with comments can contact the Coordinator, Investor Relations, the Treasurer or the Vice President and Chief Financial Officer.

   The Board also ensures that management maintains transparent communications with credit rating agencies, financial analysts and other financial market intervenors in order to fairly present the Partnership's situation. A financial information disclosure policy approved by the Board provides management with guidelines on this matter.

   **e) the integrity of the corporation's internal control and management information system.** A primary responsibility given to the Audit Committee by the Board is to satisfy itself as to the adequacy of the Partnership's internal controls and the processes for presenting financial information. To discharge this responsibility, the Committee receives periodic reports from the internal and external auditors.

2. **The board of directors should be constituted with a majority of individuals who qualify as "unrelated directors."** With the exception of the President and Chief Executive Officer, all of the directors are "unrelated," i.e. they are independent of management and are free from any interest or other relationship, other than a shareholder relationship, which could materially interfere with their ability to act in the best interests of the Partnership.

3. **The application of the definition of "unrelated director" to the circumstances of each individual director should be the responsibility of the board, which will be required to disclose on an annual basis whether the board has a majority of unrelated directors.** The Corporate Governance Committee, which is composed of unrelated outside directors, is responsible for reviewing the composition of the Board based on the definition of unrelated director. This enables the Board to ensure that it satisfies the requirements of Guideline 2.

4. **The board should appoint a committee of directors composed exclusively of outside directors, a majority of whom are unrelated directors, with the responsibility for proposing to the full board new nominees to the board and for assessing directors on an ongoing basis.** Directors are appointed either directly by the sole shareholder, or by the Board with the consent of the sole shareholder if a vacancy arises between two annual meetings. The Corporate Governance Committee reviews the composition of the Board and provides the sole shareholder with its opinion on candidates proposed by the sole shareholder or on individuals who should be considered in the Committee's view.

   From time to time, the Chairman of the Board, who also chairs the Corporate Governance Committee, discusses the individual contribution of directors with the President and Chief Executive Officer.

   During the past fiscal year, director attendance at Board and committee meetings was 88.3%, i.e. 128 attendees out of a potential 145 for 21 meetings.

5. **The board should implement a process to be carried out by the nominating committee or other appropriate committee for assessing the effectiveness of the board as a whole, the committees of the board and the contribution of individual directors.** The Board has delegated to the Corporate Governance Committee the responsibility for reviewing the methods used by the Board and its Committees for overseeing the affairs of the Company, assessing the effectiveness of the Board and its Committees in this regard and making recommendations to the Board for any improvements that could be made to corporate governance practices. To discharge this responsibility, the Committee asks directors and committee members to answer a questionnaire in a corporate governance performance self-assessment. Directors are also asked for their comments and suggestions, and for their opinion about the performance of the Chairman of the Board. The Chairman also meets with some senior executives to obtain their views on how corporate governance could be improved. The results are communicated to all of the Directors, reviewed by each committee as well as the Board, which is provided with comments and recommendations by the Corporate Governance Committee. This process is carried out every two years.

6. **Every corporation should provide an orientation and education program for new recruits to the board.** Every new director is provided with a guide that includes a description of the Company and the Partnership, a summary of the duties, obligations and responsibilities of a director as well as a copy of the mandates of the Board and its committees. Every new director is also invited to meet with each senior executive in order to acquire an understanding of each sector of activity and to get to know the executives.

   In addition, management ensures, by means of Board meeting presentations, that directors are familiar with the business of the Partnership and the industry. Management is also always available to hold information sessions for directors.

7. **Every board should examine its size, with a view to determining the impact of the number of its members upon effectiveness and, where appropriate, undertake a program to reduce the number of directors to a number which facilitates more effective decision-making.** The Board is made up of fourteen directors, seven of whom are officers of companies that are shareholders of Noverco. In view of the foregoing and the effort made to also have directors who are independent of the sole shareholder, the size of the Board appears appropriate and provides an optimal range of competencies and diverse experience.

   The Corporate Governance Committee, through its Chairman, who is also the Chairman of the Board, provides the sole shareholder with his opinion about the number of directors and the composition of the Board.

8. **The board should review the adequacy and form of the compensation of directors and ensure the compensation realistically reflects the responsibilities and risk involved in being an effective director.** The Corporate Governance Committee periodically reviews director compensation in light of the practices in comparable businesses and makes recommendations to the Board in this regard.

   Directors who receive director compensation in a personal capacity are currently required to own at least 1,000 units of the Partnership. The Board has increased this minimum to 2,000 units, effective June 1, 2004.

9. **Committees of the board of directors should generally be composed of outside directors, a majority of whom are unrelated directors.** Except for the Executive Committee, which has the President and Chief Executive Officer as a member, the Board's committees are made up solely of outside unrelated directors.

10. **The board of directors should expressly assume, or assign to a board commitee, the responsibility for developing the corporation's approach to governance issues. This committee would, among other things, be responsible for the corporation's response to the Toronto Stock Exchange guidelines.** The Corporate Governance Committee is responsible for reviewing practices followed by the Board and its committees in overseeing the management of the Company's affairs, assessing Board and committee effectiveness in this regard and making recommendations to the Board for improvements to corporate governance practices.

11. **a) The board of directors, together with the CEO, should develop position descriptions for the board and the CEO, involving the limits to management's responsibilities.** The Board adopted a written mandate that sets forth the responsibilities it reserves to itself as well as the main responsibilities delegated to the President and Chief Executive Officer. In addition, the Board has approved a written mandate for each of its committees. These mandates are part of the Guide for Directors.

    **b) The board should approve or develop the corporate objectives which the CEO is responsible for meeting.** Every year, the Human Resources Committee reviews the performance of the Partnership and of the President and Chief Executive Officer in terms of the annual and multi-year corporate objectives as well as the personal objectives agreed upon between him, the Committee and the Board. The results of the Committee's review are communicated to the Board, which also makes an overall assessment of the performance of the Partnership and of the President and Chief Executive Officer.

12. **a) Every board of directors should have in place appropriate structures and procedures to ensure the board can function independently of management. An appropriate structure would be to: (i) appoint a chair of the board who is not a member of management with responsibility to ensure the board discharges its responsibilities or (ii) adopt alternate means such as assigning this responsibility to a committee of the board or to a director, sometimes referred to as the "lead director."** Board independence is ensured by the fact that 13 out of 14 individuals are outside unrelated directors. In addition, the Board is chaired by an outside director and a written description of his responsibilities has been approved by the Board.

    **b) Appropriate procedures may involve the board meeting on a regular basis without management present or may involve expressly assigning the responsibility for administering the board's relationship to management to a committee of the board.** Outside directors hold closed-door sessions from time to time, for example, following the presentation of a strategic plan or a budget.

    In order for the Board to discharge its corporate governance responsibilities, the Corporate Governance Committee periodically reviews with management the mandates of the Board and its committees, their responsibilities, the quality of the documentation provided, the organization and frequency of meetings, follow-up of management decisions as well as communications between directors and management.

13. **a) The audit committee of every board of directors should be composed only of outside directors.** The Audit Committee is composed solely of outside directors. Their professional education and experience provide all of the Committee's members with the necessary qualifications for dealing with financial information. Two of them, including the Committee Chairman, are chartered accountants, and a third one has an MBA in finance and is a certified general accountant.

    **b) The roles and responsibilities of the audit committee should be specifically defined so as to provide appropriate guidance to audit committee members as to their duties. The audit committee duties should include oversight responsibility for management reporting on internal control. While it is management's responsibility to design and implement an effective system of internal control, it is the responsibility of the audit committee to ensure that management has done so.** The Committee is responsible for reviewing the financial information published by the Company and the Partnership, as well as how the risks that may affect the financial well-being of the organization are managed. Basically, the Committee:

- ensures there is an adequate risk management program for protecting the organization's assets;
- ensures both the external and internal auditors are independent, and approves their audit plans;
- ensures financial information transmitted to directors and the investing public is complete and objective.

    The Committee's specific responsibilities are broken down into five areas namely, external audit and external auditors, financial information, internal audit and risk management.

    **c) The audit committee should have direct communication channels with the internal and external auditors to discuss and review specific issues as appropriate.** The external auditors attend every Audit Committee meeting and, from time to time, Committee members discuss specific matters with them in closed-door sessions, i.e. without the presence of management representatives. This practice is also followed with the internal auditors, who make periodic reports to the Committee. In addition, the person responsible for internal audit meets every year with the Committee Chairman and the Board Chairman without the presence of a management representative.

14. **The board of directors should implement a system that enables an individual director to engage an outside adviser at the expense of the corporation in appropriate circumstances. The engagement of the outside adviser should be subject to the approval of an appropriate committee of the board.** Should a director wish to engage an outside consultant at the Company's expense, he (she) may do so with the prior approval of the Board or the Executive Committee or, in the case of an emergency, the Chairman of the Board.

#### MARKET INFORMATION

- Units listed on the Toronto Stock Exchange under the symbol GZM.UN.
- Unit prices for the last two fiscal years ended September 30:

| | **2002** | 2001 |
|---|---|---|
| High | **$18.32** | $16.90 |
| Low | **$16.28** | $14.80 |

- 110.5 million units outstanding with a market value of $2.0 billion as at September 30, 2002. At the same date, the market value of the 25.0 million units held by the limited Partners was $452.5 million.

#### UNIT TAX FEATURES

- Eligible investment for RRSP purposes without any restrictions. Since January 1999, investment interests in the Partnership are no longer deemed to be foreign property.
- Income is taxable as business income and Partners have to file a Québec income tax return, regardless of their province of residence.
- Partners are allocated their share of the Partnership's taxable income on a pro rata basis in accordance with distributions received. Income tax information slips (T5013 for federal purposes and *Relevé 15* for Québec purposes) are prepared and issued by the brokers. The Partnership prepares an explanatory guide for the preparation of corporate and individual income tax returns. This guide is sent with the tax information slips.
- The Partnership's income for tax purposes differs from accounting income due to differences between accounting principles and tax legislation. On average, since 1993, income for tax purposes has exceeded distributions by 7.4% for federal purposes and 6.6% for Québec purposes. Historically, the differences have been as high as +26.8% (unfavourable variance for a taxable partner) and as low as –18.1% (favourable variance for a taxable partner). For the year ended September 30, 2002, income for tax purposes exceeded distributions by 26.8% for federal purposes and 26.4% for Québec purposes. Partners that hold their units in a non-taxable vehicle, such as an RRSP, are in no way affected by the difference between income for tax purposes and distributions received.
- Partners who are not resident in Canada must file both a federal and Québec income tax return and, under the terms of the Partnership Agreement, a Partner who is a "non-resident" of Canada can be required to sell his units to a person who is not a "non-resident".

#### INCOME DISTRIBUTIONS

- Policy is to distribute virtually all of the income in each fiscal year.
- Quarterly distributions are paid on January 1, April 1, July 1 and October 1 to Partners of record at the close of business on December 15, March 15, June 15 and September 15 of each year.
- The Partnership approved a quarterly distribution of $0.34 per unit payable on January 1, 2003.
- Partners may request that their income distributions be deposited directly into a Canadian bank account. This rapid, reliable and convenient service is offered by most banks and other financial institutions. To take advantage of this direct deposit service, contact CIBC Mellon at 1 800 387-0825.

#### GENERAL INFORMATION

TRANSFER AGENT: CIBC Mellon.

ANNUAL MEETING: The Partnership's annual meeting of Partners will be held at 2:00 p.m., Friday, February 21, 2003, at the Hilton Bonaventure Hotel, Salon Outremont, 1, Place Bonaventure, Montréal, Québec.

PUBLICATION OF RESULTS: Following approval by the Board of Directors, the quarterly results will be published around the following dates:

| | |
|---|---|
| 1st quarter: February 21, 2003 | 3rd quarter: August 20, 2003 |
| 2nd quarter: May 21, 2003 | 4th quarter: November 19, 2003 |

INVESTOR RELATIONS: 1717 du Havre Street, Montréal, Québec H2K 2X3 Telephone: (514) 598-3324 or (514) 598-3534 Fax: (514) 521-8168 E-mail: investors@gazmet.com

Quarterly reports, annual report and press releases are accessible through our Internet site: **www.gazmetro.com**

## BOARD OF DIRECTORS

**J. RICHARD BIRD**[1]
Group Vice President
Transportation North
Enbridge Inc.

**JEAN-GUY DESJARDINS**[3]
President and
Chief Executive Officer
Fiera Capital Inc.

**NICOLLE FORGET**[3,4,5]
Corporate Director

**LOUIS P. GIGNAC**[1,4,5]
President and
Chief Executive Officer
Cambior Inc.

**MICHEL GOURDEAU**[1,2]
Executive Vice President
Natural Gas Sector
Hydro-Québec

**EMMANUEL HEDDE**
Executive Vice President
Finance Division
Gaz de France

**PHILIPPE HOCHART**[1]
Representative for
North America
Gaz de France

**JACQUES LAURENT**[4]
(Vice Chairman)
Chairman of the Board
Hydro-Québec

**STEPHEN J.J. LETWIN**[2]
Group Vice President
Distribution and Services
Enbridge Inc.

**GASTON LONGVAL**[3]
Corporate Director

**MICHEL MARUENDA**
Deputy Executive
Vice President
EDF GDF Services

**ROBERT PARIZEAU**[1,2,3,4,5]
(Chairman of the Board)
Chairman of the Board
Aon Parizeau Inc.

**RÉAL SUREAU**[2,3,5]
President
Gestion Sureau Limitée

**ROBERT TESSIER**[1]
President and
Chief Executive Officer
Gaz Métropolitain, inc.

## MANAGEMENT

**ROBERT TESSIER**
President and
Chief Executive Officer

**RENÉ BÉDARD**
Corporate Secretary

**STÉPHANE BERTRAND**
Vice President
Communications, Public
and Governmental Affairs

**ANDRÉ BOULANGER**
Vice President
Sales, Marketing
and Customer Services

**SOPHIE BROCHU**
Vice President
Business Development
and Gas Supply

**JACQUES CHARRON**
Vice President
Operations

**PIERRE DESPARS**
Vice President
Corporate and
Legal Affairs

**SERGE RÉGNIER**
Vice President
Human Resources
and Quality

**LUC SICOTTE**
Vice President and
Chief Financial Officer

1 Member of the Executive Committee
2 Member of the Audit Committee
3 Member of the Pension Fund Committee
4 Member of the Human Resources Committee
5 Member of the Corporate Governance Comittee

## BUSINESS OFFICES

### GAZ MÉTROPOLITAIN

**HEAD OFFICE**
1717 du Havre Street
Montréal, Québec
H2K 2X3
(514) 598-3444

**BUSINESS OFFICE–WEST**
2200 de Cannes-Brûlées Street
Lasalle, Québec
H8N 2Z2
(514) 367-6800

**BUSINESS OFFICE–EAST**
11401 L.-J. Forget Avenue
Anjou, Québec
H1J 2Z8
(514) 356-8777

**ABITIBI-TÉMISCAMINGUE**
145 Québec Boulevard
Rouyn-Noranda, Québec
J9X 6M8
(819) 797-2111

**EASTERN TOWNSHIPS**
240 Léger Street
Sherbrooke, Québec
J1L 1M1
(819) 564-1311

**LAURENTIANS**
905 Michèle-Bohec Street
Blainville, Québec
J7C 5E7
(450) 434-4091

**MAURICIE**
929 Père-Daniel Street
Trois-Rivières, Québec
G9A 2W9
(819) 372-1242

**MONTÉRÉGIE**
3657 Isabelle Street
Brossard, Québec
J4Y 2R2
(450) 659-7674

**QUÉBEC**
2300 Jean-Perrin Street
Québec, Québec
G2C 1K8
(418) 842-9960

**SAGUENAY–LAC-SAINT-JEAN**
1100 Bersimis Street
Chicoutimi, Québec
G7K 1A5
(418) 696-2231

### SUBSIDIARIES AND AFFILIATES

**GAZ MÉTROPOLITAIN PLUS INC.**
1350 Nobel Street
Boucherville, Québec
J4B 5H3
(450) 641-6300
*André Gougeon*
*President and Chief Executive Officer*

**CONSULGAZ INC.**
1350 Nobel Street
Boucherville, Québec
J4B 5H3
(450) 641-8604
*André Gougeon*
*President and Chief Executive Officer*

**CCUM, S.E.C.**
1350 Nobel Street
Boucherville, Québec
J4B 5H3
(450) 641-8389
*André Gougeon*
*President and Chief Executive Officer*

**SOGENER INC.**
1350 Nobel Street
Boucherville, Québec
J4B 5H3
(450) 641-8356
*André Gougeon*
*President and Chief Executive Officer*

**VDN CABLE INC.**
2600 Ontario Street East
Suite 152
Montréal, Québec
H2K 4K4
(514) 522-1590
*Philip Gale*
*President*

**OPTION GAZ LTD**
1800 TransCanada Highway
Dorval, Québec
H9P 1H7
(514) 421-7992
*André Gougeon*
*President and Chief Executive Officer*

**TELDIG SYSTEMS INC.**
575 Saint Joseph Street East
Québec, Québec
G1K 3B7
(418) 948-1314
1-800-501-5554
*Jacques Therrien*
*President*

**TRANS QUÉBEC & MARITIMES PIPELINE INC.**
6200 Taschereau Boulevard
2nd floor
Brossard, Québec
J4W 3J8
(450) 462-5301
*Réjean Laforge*
*President*

**VERMONT GAS SYSTEMS, INC.**
85 Swift Street
South Burlington
Vermont 05403
(802) 863-8899
*A. Donald Gilbert*
*President and Chief Executive Officer*

**SOFAME TECHNOLOGIES INC.**
500 Alphonse-D.-Roy Street
Montréal, Québec
H1W 3Y8
(514) 523-6545
*Charles Delisle*
*President–General Manager*

**AQUA-REHAB INC.**
2145 Michelin Street
Laval, Québec
H7L 5B8
(450) 687-3472
*Georges Dorval*
*President*

**AQUA DATA INC.**
95–5th Avenue
Pincourt, Québec
J7V 5K8
(514) 425-1010
*Gordon Halliday*
*President*

**CHAMPION PIPE LINE CORPORATION LIMITED**
1717 du Havre Street
Montréal, Québec
H2K 2X3
(514) 598-3444
Jacques Charron
President

**PORTLAND NATURAL GAS TRANSMISSION SYSTEM**
One Harbour Place
Suite 375
Portsmouth
New Hampshire 03801
USA
(603) 559-5509
*Richard H. Leehr*
*President*

**CLIMTECH INC.**
12020 Albert-Hudon Blvd
Montréal-Nord, Québec
H1G 3K7
(514) 353-2259
*André Gougeon*
*President and Chief Executive Officer*

**SERVITECH COMBUSTION INC.**
12020 Albert-Hudon Blvd
Montréal-Nord, Québec
H1G 3K7
(514) 353-6732
*André Gougeon*
*President and Chief Executive Officer*

**CARTIER PIPELINE INC.**
1717 du Havre Street
Montréal, Québec
H2K 2X3
(514) 598-3768
Juri Otsason
President

**GAZ MÉTROPOLITAIN WANTS TO THANK FOR THEIR COLLABORATION**
Au Petit Extra, 1690, Ontario East Street, Montreal; Multimags, 3552, Saint Lawrence Boulevard, Montreal.

Photographer: Yves Beaulieu

**CE DOCUMENT EST DISPONIBLE EN FRANÇAIS.**

Design: www.nolin.ca Printed in Canada

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